

No. 10183

United States.

Circuit Court of Appeals

For the Ninth Circuit.

LANE-WELLS COMPANY, a corporation, and
TECHNICRAFT ENGINEERING—COR-
PORATION,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Transcript of the Record

Upon Petitions to Review a Decision of the
United States Board of Tax Appeals

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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APPEARANCES

For Taxpayer:

RAPHAEL DECHTER, Esq.,

J. R. WHITE, C. P. A.

For Commissioner:

E. A. TONJES, Esq.,

ALVA C. BAIRD, Esq.

DOCKET NO. 99829

LANE-WELLS COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

1939

Aug. 22—Petition received and filed. Taxpayer notified. Fee paid.

Aug. 22—Copy of petition served on General Counsel.

Oct. 18—Answer filed by General Counsel.

Oct. 18—Request for Circuit hearing in Los Angeles, Calif., filed by General Counsel.

Oct. 21—Notice issued placing proceeding on Los Angeles calendar. Answer and request served.

1940

May 14—Hearing set June 3, 1940 at Los Angeles, Calif.

Jun. 5-6—Hearing had before Mr. Black on merit. Submitted. Motion to consolidate for hearing with 99830 granted. Continued to June 6, 1940. Petitioner's brief due 8/6/40, respondent's 9/6/40. Reply 10/5/40.

1940

Jul. 1—Transcript of hearing of June 5, 1940 filed.

Jul. 1—Transcript of hearing of June 6, 1940 filed.

Aug. 5—Brief filed by taxpayer, 8/5/40 copy served.

Sep. 6—Brief filed by General Counsel.

Oct. 3—Reply brief filed by taxpayer. 10/4/40. copy served.

1941

Jan. 31—Findings of fact and opinion rendered, Black. Decision will be entered under Rule 50.

Apr. 23—Joint motion to open record and for the introduction of further evidence filed.

May 12—Order granting motion to open record and for the introduction of further evidence entered.

May 29—Stipulation of facts filed.

May 29—Joint motion for extension of 30 days from June 4, 1941 to file briefs and 20 days thereafter to file reply briefs filed. 5/31/41 granted.

Jun. 21—Memorandum brief filed by taxpayer. 7/7/41 copy served.

Jul. 3—Supplemental memorandum brief filed by General Counsel.

1941

Jul. 23—Reply brief filed by taxpayer. 7/23/41 copy served.

Sep. 25—Supplemental opinion rendered, Black. Decision will be entered under Rule 50. 9/25/41 copy served.

Oct. 22—Computation of deficiency filed by General Counsel.

Oct. 25—Hearing set 11/12/41 on settlement.

Nov. 4—Computation of deficiency filed by taxpayer.

Nov. 19—Decision entered, Black, Div. 15. [1*]

1942

Feb. 11—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, with assignments of error filed by General Counsel.

Feb. 16—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit with assignments of error filed by taxpayer.

Feb. 25—Proof of service of filing petition for review filed by General Counsel. (2)

Feb. 27—Proof of service of filing petition for review filed by taxpayer.

Mar. 18—Certified copy of order from the 9th Circuit extending the time to June 22, 1942 for the preparation and transmission of the record filed. (Both causes.)

Mar. 27—Certified copy of order from the 9th Circuit re consolidation with docket 99830 filed. (Both causes.)

*Page numbering appearing at top of page of original Reporter's Transcript.

1942

June 15—Mandate from U. S. Circuit Court of Appeals, 9th Circuit, dismissing appeal filed. (Commissioner's.)

June 15—Agreed statement of evidence filed.

June 15—Agreed praecipe filed.

June 19—Order re the transmission of exhibits 6, 7, 8, 9, 10, 11, 12 and 13 in their original form entered, Mr. Black, Div. 15.

June 22—Certified copy of an order from the 9th Circuit extending the time to July 22, 1942 to prepare and transmit the record filed. [2]

DOCKET NO. 99830

TECHNICRAFT ENGINEERING CORPORATION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

1939

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Mar. 27—Certified copy of order from the 9th Circuit re consolidation with docket 99829 filed. (Both causes.)

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June 15—Agreed statement of evidence filed.

June 15—Agreed praecipe filed.

June 19—Order re the transmission of exhibits 6, 7, 8, 9, 10, 11, 12 & 13 in their original form entered, Mr. Black, Div. 15.

June 22—Certified copy of an order from the 9th Circuit extending the time to July 22, 1942 to prepare and transmit the record filed. [4]

United States Board of Tax Appeals

Docket No. 99829

LANE-WELLS COMPANY,

Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

PETITION

The above-named petitioner hereby petitions for

a redetermination of the liability as transferee set forth by the Commissioner of Internal Revenue in his notice of liability as transferee (Bureau symbols IT:LA:FHG-90D) dated June 1, 1939, and as a basis for its proceeding alleges as follows:

1. The petitioner is a corporation organized under the laws of the State of Delaware, with its principal office at 5610 South Soto Street, Los Angeles, California.

2. The notice of liability as transferee (a copy of which it attached and marked Exhibit A) was mailed to the petitioner on June 1, 1939.

3. The Commissioner proposes for assessment against the petitioner the amount of \$74,647.41 alleging that said amount constitutes the petitioner's liability as transferee of the assets of Technicraft Engineering Corp., 5610 South Soto Street, Los Angeles, California, for normal income tax, surtax on personal holding companies and penalty of 25% of surtax on personal holding companies as follows: [5]

Year ending December 31	Normal income tax	Surtax on undistributed profits	Surtax on personal holding companies	Penalty of 25% of surtax on personal holding companies
1934			\$ 3,178.80	\$ 794.70
1935			9,474.53	2,368.63
1936			5,115.11	1,278.78
1937	\$ 553.65	\$ 643.15	40,992.05	10,248.01
Total	<u>\$ 553.65</u>	<u>\$ 643.15</u>	<u>\$58,760.49</u>	<u>\$14,690.12</u>
Proposed assessment				<u><u>\$74,647.41</u></u>

Corp., 5610 South Soto Street, Los Angeles, California, for the taxable years ended December 31, 1936 and December 31, 1937, discloses a deficiency of \$1,196.80 for the taxable year ended December 31, 1937 and an overassessment of \$21.82 for the taxable year ended December 31, 1936; and that the determination of the personal holding company surtax liability of the said Technicraft Engineering Corp. for the taxable years ended December 31, 1934, December 31, 1935, December 31, 1936, and December 31, 1937, discloses a deficiency of \$58,760.49 and \$14,690.12 in penalty; as shown in the statement attached. The amount of the deficiencies and penalty stated, plus interest as provided by law, constituting your liability as transferee of assets of said Technicraft Engineering Corp., will be assessed against you. The overassessment, to the extent that it represents an overpayment of tax, will be credited in the manner provided by law.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of his letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge,

18.

Lane-Wells Co. et al vs.

Los Angeles, California, for the attention of IT: LA-FC. The signing and filing of this form will expedite the closing of your case by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,

Commissioner,

(Signed) By GEORGE D. MARTIN

Internal Revenue Agent
in Charge.

Enclosures:

Statement.

Form of waiver and acceptance. [12]

Lane-Wells Company, Transferee,
Los Angeles, California.

STATEMENT.

IT:LA

FHG-90D

Technicraft Engineering Corp.,
Transferor.

5610 South Soto Street,
Los Angeles, California.

Tax Liability for the Taxable Years Ended
December 31, 1934,
December 31, 1935,
December 31, 1936,
and
December 31, 1937.

Lane-Wells Company,
Transferee,
5610 South Soto Street,
Los Angeles, California.

Taxable Year	Liability	Assessed	Deficiency	Over-assessment
INCOME TAX				
Ended Dec. 31, 1936.....	\$24,479.03	\$24,500.85	\$ None	\$21.82
Ended Dec. 31, 1937.....	28,200.51	27,003.71	1,196.80	None
Totals, income tax.....	\$56,679.54	\$51,504.56	\$1,196.80	\$21.82

PERSONAL HOLDING COMPANY SURTAX				
Ended Dec. 31, 1934.....	\$ 3,178.80	None	\$ 3,178.80	None
Ended Dec. 31, 1935.....	9,474.53	None	9,474.53	None
Ended Dec. 31, 1936.....	5,115.11	None	5,115.11	None
Ended Dec. 31, 1937.....	40,992.05	None	40,992.05	None
Totals, personal holding company surtax.....	\$58,760.49	None	\$58,760.49	None

25% PENALTY, PERSONAL HOLDING COMPANY

Ended Dec. 31, 1934.....	\$ 794.70	None	\$ 794.70	None
Ended Dec. 31, 1935.....	2,368.63	None	2,368.63	None
Ended Dec. 31, 1936.....	1,278.78	None	1,278.78	None
Ended Dec. 31, 1937.....	10,248.01	None	10,248.01	None
Totals, 25% penalty.....	\$14,690.12	None	\$14,690.12	None

[13]

The records of this office indicate that the Technicraft Engineering Corp., 5610 South Soto Street, Los Angeles, California, has been dissolved and that assets were transferred to you on or about August 31, 1937.

The above-mentioned amounts represent your liability as a transferee of assets of the Technicraft

Engineering Corp., 5610 South Soto Street, Los Angeles, California, for deficiencies of income tax and personal holding company surtax due from the Technicraft Engineering Corp. for the taxable years ended December 31, 1934, 1935, 1936, and 1937.

[Endorsed]: U. S. B. T. A. Filed Aug. 22, 1939. [14]

[Title of Board and Cause—Docket No. 99829.]

ANSWER

Comes now the respondent, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed in the above-entitled proceeding, admits, denies, and alleges as follows:

1. Admits the allegations contained in paragraph 1 of the petition.
2. Admits the allegations contained in paragraph 2 of the petition.
3. Admits that the Commissioner proposed for assessment against the petitioner, as a transferee of Technicraft Engineering Corp., deficiencies in income taxes for the year 1937 in the amount of \$1,196.80, a deficiency in personal holding company surtaxes in the amount of \$58,760.49 for the years 1934 to 1937, inclusive, a penalty of 25% of the personal holding company sur- [15] tax for the

years 1934 to 1937, inclusive. Denies the remainder of the allegations contained in paragraph 3 of the petition.

4. (a) to (l), inclusive. Denies the allegations of error set forth in subparagraphs (a) to (l), inclusive, of paragraph 4 of the petition.

5. (a) Admits that Technicraft Engineering Corp. was organized under the laws of California in the year 1932. Denies the remainder of the allegations contained in subparagraph (a) of paragraph 5 of the petition.

(b) to (e), inclusive. Denies the allegations contained in subparagraphs (b) to (e), inclusive, of paragraph 5 of the petition.

(f) Admits that Technicraft Engineering Corp. was liquidated and all of its assets transferred to this petitioner and that the Technicraft Engineering Corp. was dissolved. Denies the remainder of the allegations contained in subparagraph (f) of paragraph 5 of the petition.

(g) to (o), inclusive. Denies the allegations contained in subparagraphs (g) to (o), inclusive, of paragraph 5 of the petition.

6. Denies generally and specifically each and every allegation contained in the petition not hereinbefore admitted, qualified, or denied. [16]

Further answering, respondent alleges:

7. That within the time required by law the Commissioner of Internal Revenue mailed a notice of deficiency to Technicraft Engineering Corp., asserting a deficiency in income taxes for the year

1937 in the amount of \$1,196.80, and deficiencies in personal holding company surtaxes for the years 1934 to 1937, inclusive, in the respective amounts of \$3,178.80, \$9,474.53, \$5,115.11, and \$40,992.05, plus a penalty of 25% of the foregoing amounts for failure to file a personal holding company return in the respective amounts of \$797.70, \$2,368.63, \$1,278.78, and \$10,248.01.

8. That thereafter a petition praying for a redetermination of the asserted deficiencies was filed with the United States Board of Tax Appeals by Technicraft Engineering Corp. and bears Docket No. 99830 and is now pending before the said Board.

9. That no part of the asserted deficiencies in income taxes, personal holding company surtaxes, penalties and interest for the years 1934 to 1937, inclusive, has been paid and the entire amounts still remain outstanding and unpaid.

10. That subsequent to the date that the said income taxes, personal holding company surtaxes, penalties and interest became due, the Technicraft Engineering Corp. distributed all of its properties and assets to this petitioner. [17]

11. That said property and assets distributed by the Technicraft Engineering Corp. to this petitioner had a value in excess of the income taxes, personal holding company surtaxes, penalties and interest, as provided by law, involved in this proceeding.

12. That the Technicraft Engineering Corp. has since discontinued its business and dissolved.

13. That the transfer of all of its property and assets by the Technicraft Engineering Corp. to this petitioner was without consideration.

14. That this petitioner assumed and agreed to pay all of the liabilities of the Technicraft Engineering Corp., including its liability for Federal income, personal holding company surtax, penalties and interest for the years 1934 to 1937, inclusive.

Wherefore, it is prayed that the petitioner's appeal be denied, that the respondent's determination be approved, and that the petitioner be held to be liable at law and in equity as a transferee of the assets of the Technicraft Engineering Corp. in the amounts shown in the notice of deficiency from which this appeal was taken, together with interest thereon as provided by law.

Signed

J. P. WENCHEL

FTH

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

ALVA C. BAIRD,

FRANK T. HORNER,

E. A. TONJES,

Special Attorneys,

Bureau of Internal Revenue.

EAT:E 10/12/39

[Endorsed]: U. S. B. T. A. Filed Oct. 18,
1939. [18]

United States Board of Tax Appeals
Docket No. 99830

TECHNICRAFT ENGINEERING CORP.,

Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Bureau symbols IT:LA:FHG-90D) dated June 1 1939, and as a basis for its proceeding alleges as follows:

1. The petitioner is a corporation organized under the laws of the State of California, with its principal office at 5610 South Soto Street, Los Angeles, California.

2. The notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner on June 1 1939:

3. The taxes in controversy are normal income tax, surtax on personal holding companies and penalty of 25% of surtax on personal holding companies as follows:

Year ending December 31	Normal income tax	Surtax on undistributed profits	Surtax on personal holding companies	Penalty of 25% of surtax on personal holding companies
1934			\$ 3,178.80	\$ 794.70
1935			9,474.53	2,368.63
1936			5,115.11	1,278.78
1937	\$553.65	\$643.15	40,992.05	10,248.01
Total....	\$553.65	\$643.15	\$58,760.49	\$14,690.12
Proposed assessment				\$74,647.41

[19]

The petitioner claims that it is entitled to refund of overpayments of normal income tax for 1937 of \$7,483.16 and of surtax on undistributed profits for 1937 of \$10,248.87 making a total amount in controversy of \$92,379.44.

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) The Commissioner erred in determining that petitioner was a "personal holding company" for each of the years 1934 to 1937 inclusive.

(b) The Commissioner erred in failing to determine that the amounts of petitioner's income designated "royalties" were in fact compensation for tangible services rendered to affiliated corporations and as such did not constitute "personal holding company" income.

(c) The Commissioner erred in determining

that the failure of petitioner to file Form 1120-H for each of the years 1934 to 1937 inclusive was not due to reasonable cause.

(d) The Commissioner erred in asserting penalties of 25% of the surtax on personal holding companies for delinquency in filing Form 1120-H for each of the years 1934 to 1937 inclusive.

(e) The Commissioner erred in failing to determine that the period for assessment of any deficiency or penalty in respect of the 1934 income of petitioner had expired prior to the issuance of the deficiency notice.

(f) The Commissioner erred in failing to determine that the period for assessment of any deficiency or penalty in respect of the 1935 income of petitioner had expired prior to the issuance of the deficiency notice.

(g) In determining the liability of petitioner for surtax on undistributed profits and for surtax on personal holding companies in respect of its 1937 income, the Commissioner erred in not allowing a "dividends paid credit" for amounts distributed during 1937 in final and complete liquidation of petitioner. [20]

(h) The Commissioner erred in failing to determine that there was an overassessment of surtax on undistributed profits against petitioner for 1937 of \$10,248.87.

(i) The Commissioner erred in failing to determine that the income and deductions re-

ported by petitioner for the period from June 1 1937 to August 31 1937 in fact constituted income and deductions of Lane-Wells Company, the successor corporation and not income and deductions of petitioner.

(j) The Commissioner erred in failing to determine that there was an overassessment of normal income tax against petitioner for 1937 of \$7,483.16.

(k) The Commissioner erred in failing to recognize that by his past acts and conduct he is estopped from asserting any claim of liability against petitioner for surtax on personal holding companies or penalties thereon.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) Petitioner was organized under the laws of California in 1932 to conduct the engineering, experimental and development work of the group of affiliated companies of which it was a member.

(b) In order to provide petitioner with funds to carry out its functions, the other companies paid to petitioner amounts which have been designated as "royalties" as consideration for experimental work, for engineering services and for the use of patents and inventions but no part of these amounts constituted a payment of income in respect of investments in such patents and inventions. The use of the word "royalties" was not intended to give that

word any legal effect and neither the use of the word "royalties" nor the payments of amounts designated as "royalties" was intended to measure a return on investments in assets such as patents and inventions but the word was used as a convenience to designate the compensation paid to petitioner for services rendered. [21]

(c) Because of the identical stock interests of the shareholders of petitioner with their interests in the other companies the so-called royalties were not determined in accordance with the value of the services rendered but in an amount deemed necessary to provide the funds required to carry on the development work.

(d) These so-called royalties were not royalties in fact and did not constitute personal holding company income.

(e) Petitioner's last taxable year was the calendar year 1937.

(f) Pursuant to a plan of reorganization, petitioner was liquidated effective as of May 31, 1937, all of its assets being transferred to Lane-Wells Company in consideration of the issuance of stock of that company to the former stockholders of petitioner which was dissolved as soon thereafter as possible, the date of the certificate of dissolution being October 22 1937. Since, as a result of its reorganization, all of the assets and stock of petitioner were

transferred effective as of May 31 1937, petitioner, subsequent to that date, had no shareholders within the meaning of Section 351 of the Revenue Act of 1936.

(g) During the last half of 1937 more than 50% in value of the outstanding stock of petitioner was not owned directly or indirectly by or for five or less individuals.

(h) The failure of petitioner to file Form 1120-H for each of the years 1934 to 1937 inclusive was due to reasonable causes and not due to negligence or to any intent to defeat or avoid payment of tax.

(i) Petitioner in good faith filed its regular tax returns (Form 1120) for 1934 on or about March 15 1935, for 1935 on or about March 15, 1936, for 1936 on or about March 15 1937 and for 1937 on or about March 15 1938, all within the time prescribed by law. Petitioner's officers believed that it was not a "personal holding company" and so stated in the returns. This belief was substantiated by the fact that the returns for 1934 and 1935 were examined by representatives of the Treasury Department who apparently agreed that petitioner was not a "personal holding company" as no attempt was made to assert such surtax and a refund of 1935 income and excess-profits taxes was approved in the amount of \$278.47 which was received by petitioner on June 19 1937. In view of such acts and conduct the

Commissioner is now estopped from asserting that petitioner was a "personal holding company." [22]

(j) The time for assessment against petitioner of additional tax and penalties in respect of its 1934 income expired three years after its 1934 return was filed or on or about March 15 1938.

(k) The time for assessment against petitioner of additional tax and penalties in respect of its 1935 income expired three years after its 1935 return was filed or on or about March 15 1939.

(l) Of the amounts distributed in liquidation of petitioner not less than \$65,814.75 was properly chargeable to earnings and profits accumulated subsequent to February 28 1913 and in determining the surtax on undistributed profits and the surtax on personal holding companies of petitioner for 1937 a "dividends paid credit" in this amount should be allowed.

(m) The income tax return filed by petitioner for 1937 included net income of \$49,887.61 for the period from June 1 1937 to August 31 1937 which was in fact net income of Lane-Wells Company, the successor corporation. Petitioner's net income for 1937 was \$69,544.63.

(n) Petitioner paid \$16,754.84 normal income tax and \$10,248.87 surtax on undistrib-

uted profits tax for 1937 on or about the following dates:

March	15 1938	\$ 6,750.93
June	15 1938	6,750.93
September	15 1938	6,750.93
December	15 1938	6,750.92

\$27,003.71

Wherefore, the petitioner prays that this Board may hear the proceeding and determine:

(a) That there is no deficiency due from petitioner for normal income tax, surtax on personal holding companies or penalties thereon for each of the years 1934 to 1937 inclusive. [23]

(b) That there are overpayments by petitioner of normal income tax for 1937 in the amount of \$7,483.16 and of surtax on undistributed profits for 1937 in the amount of \$10,248.87; that such amounts were paid by petitioner within three years before the filing of this petition and that petitioner is entitled to refund of these overpayments.

Los Angeles, California, August 11, 1939.

RAPHAEL DECHTER,

Counsel for Petitioner,

417 South Hill Street,

Los Angeles, California.

J. R. WHITE,

Agent for Petitioner,

530 West Sixth Street,

Los Angeles, California.

[24]

(Duly verified.) [25]

EXHIBIT A.

TREASURY DEPARTMENT

Internal Revenue Service

12th Floor,

U. S. Post Office and Court House,
Los Angeles, California.

JUN 1 1939

Office of
Internal Revenue Agent

in Charge

Los Angeles Division

IT: LA

FHG-90D

Technicraft Engineering Corp.,

5610 South Soto Street,

Los Angeles, California.

Sirs:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1936 and December 31, 1937, discloses a deficiency of \$1,196.80 for the taxable year ended December 31, 1937 and an overassessment of \$21.82 for the taxable year ended December 31, 1936; and that the determination of your personal holding company surtax liability for the taxable years ended December 31, 1934, December 31, 1935, December 31, 1936 and December 31, 1937, discloses a deficiency of \$58,760.49 and \$14,690.12 in penalty; as shown in the statement attached.

In accordance with the provisions of existing in-

ternal revenue laws, notice is hereby given of the deficiency mentioned.

Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in-Charge, Los Angeles, California, for the attention of IT: LA-FC. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,

Commissioner,

By (Signed) GEORGE D. MARTIN

Internal Revenue Agent in
Charge.

Enclosures:

Statement.

Form of waiver and acceptance.

Claim. [26]

STATEMENT.

IT: LA

FHG-90D

Technicraft Engineering Corp.,

5610 South Soto Street,

Los Angeles, California.

Tax Liability for the Taxable Years Ended

December 31, 1934,

December 31, 1935,

December 31, 1936,

and

December 31, 1937.

Taxable year	Liability	Assessed	Deficiency	Over-assessment
INCOME TAX				
Ended Dec. 31, 1936....	\$24,479.03	\$24,500.85	\$ None	\$21.82
Ended Dec. 31, 1937....	28,200.51	27,003.71	1,196.80	None
Totals, income tax....	\$52,679.54	\$51,504.56	\$1,196.80	\$21.82

PERSONAL HOLDING COMPANY SURTAX

Ended Dec. 31, 1934....	\$ 3,178.80	None	\$ 3,178.80	None
Ended Dec. 31, 1935....	9,474.53	None	9,474.53	None
Ended Dec. 31, 1936....	5,115.11	None	5,115.11	None
Ended Dec. 31, 1937....	40,992.05	None	40,992.05	None
Totals, personal holding company surtax.....	\$58,760.49	None	\$58,760.49	None

25% PENALTY, PERSONAL HOLDING COMPANY

Ended Dec. 31, 1934....	\$ 794.70	None	\$ 794.70	None
Ended Dec. 31, 1935....	2,368.63	None	2,368.63	None
Ended Dec. 31, 1936....	1,278.78	None	1,278.78	None
Ended Dec. 31, 1937....	10,248.01	None	10,248.01	None
Totals, 25% penalty.	\$14,690.12	None	\$14,690.12	None

In making this determination of your income tax liability, and liability for personal holding company surtax and penalty, careful consideration has been given to the reports of examination dated October 21, 1938(2) and January 27, 1939; to your protests dated November 17, 1938, February 6, 1939 and February 18, 1939; and to the statements made at the conferences held on December 1, 1938 and March 20, 1939.

Inasmuch as you failed to file returns of personal holding company subject to surtax under Section 351 of the Revenue Acts of 1934 and 1936 as amended by Section 1 of the Revenue Act of 1937, within the time prescribed by law, 25 per centum of the surtax has been added thereto in accordance with the provisions of Sections 291 of the Revenue Acts of 1934 and 1936 and Section 406 of the Revenue Act of 1935.

The contention raised in your protest dated February 18, 1939, to the effect that the limitation provided by Section 275(a) of the Revenue Act of 1934 has interposed to prevent the assessment of the personal holding company surtax imposed by Section 351 of the said Revenue Act, is denied for the reason that you failed to file the return required by Section 351(c), and it is provided in Section 276(a) that in the event of such failure the tax may be assessed at any time.

The overassessment shown herein will be made the subject of a certificate of overassessment which will reach you in due course through the office of

the collector of internal revenue for your district, and will be applied by that official in accordance with Section 322 of the Revenue Act of 1936, provided that you fully protect yourself against the running of the statute of limitations with respect to the apparent overassessment referred to in this letter, by filing with the collector of internal revenue for your district, a claim for refund on form 843, a copy of which is enclosed, the basis of which may be as set forth herein.

If you do not acquiesce in all of the adjustments making up the deficiency indicated, but desire to stop the accumulation of interest on that part of the deficiency resulting from adjustments to which you agree, please fill out the enclosed form of waiver, inserting therein the amount of the deficiency you desire to have assessed at once. The execution of the form for the agreed portion of the deficiency will not deprive you of your right to petition the United States Board of Tax Appeals for a redetermination of the deficiency. [28]

A copy of this letter and statement has been mailed to your representative, Mr. D. S. Jeppson, 639 South Spring Street, Los Angeles, California, in accordance with the authority contained in the power of attorney executed by you and on file with the Bureau.

ADJUSTMENTS TO NET INCOME.

Taxable year ended December 31, 1934.

Net income as disclosed by return on Form 1120,....		\$15,732.99
Additional deductions:		
(a) Additional capital stock tax.....	\$ 15.00	
(b) Amortization of patents.....	309.69	324.69
		<hr/>
Net income adjusted.....		\$15,408.30

EXPLANATION OF ADJUSTMENTS.

(a) The allowable deduction for Federal capital stock tax is represented by the amount of \$265.00 which accrued and became a liability on July 1, 1934, in lieu of the amount of \$250.00 paid in the taxable year and claimed as a deduction in the return.

(b) An allowable deduction of \$309.69 for amortization of patents was charged to surplus account in error and was not claimed in the return filed.

It is held that for the taxable year you were a personal holding company as defined in Section 351 (b) (1) of the Revenue Act of 1934, and are subject to the surtax imposed by Section 351(a) of such Revenue Act.

Since you failed to file a personal holding company return as required by Section 351(c) of the Revenue Act of 1934, the imposition of the 25% penalty imposed by Section 291 is mandatory.

Since the provisions of Sections 275 and 322 of the Revenue Act of 1934 operate to prevent any adjustment of your income tax liability, the computation of tax liability herein is limited to your liability for the personal holding company surtax and penalty above mentioned. [29]

COMPUTATION OF TAX.

Taxable year ended December 31, 1934.

PERSONAL HOLDING COMPANY SURTAX.

Taxable net income,.....	\$15,408.30
Less: Federal income and profits taxes,.....	2,163.29
Adjusted net income,.....	\$13,245.01
Less: 20 per cent of adjusted net income,.....	2,649.00
Undistributed adjusted net income,.....	\$10,596.01
Surtax:	
30% of \$10,596.01.....	\$ 3,178.80
Penalty of 25% for delinquency; Section 291.....	974.70
Deficiency of personal holding company surtax and penalty,	\$ 3,973.50

ADJUSTMENT TO NET INCOME.

Taxable year ended December 31, 1935.

Net income as disclosed by return on Form 1120,.....	\$48,028.20
Additional deduction:	
Accrued capital stock tax.....	1,485.00
Net income adjusted,.....	\$46,543.20

EXPLANATION OF ADJUSTMENT.

The allowable deduction for Federal capital stock tax is represented by the amount of \$1,750.00 which accrued and became a liability on July 1, 1935, in lieu of the amount of \$265.00 paid in the taxable year and claimed as a deduction in the return.

It is held that, for the taxable year you were a personal holding company as defined in Section 351 (b) (1) of the Revenue Act of 1934, and are subject to the surtax imposed by Section 351(a) of such Revenue Act.

Since you failed to file a personal holding company return as required by Section 351(c) of the Revenue Act of 1934, the imposition of the 25%

penalty imposed by Section 406 of the Revenue Act of 1935 is mandatory. [30]

The adjustment to net income noted above resulted in an overassessment of income tax in an amount of \$204.22 and an overassessment of excess-profits tax in an amount of \$74.25, which have previously been made the subject of appropriate action in accordance with acceptance signed by you on October 2, 1936; in view of which the computation of tax liability herein is limited to your liability for the personal holding company surtax and penalty above mentioned.

COMPUTATION OF TAX.

Taxable year ended December 31, 1935.

PERSONAL HOLDING COMPANY SURTAX.

Taxable net income.....	\$46,543.20
Less: Federal income and profits taxes.....	7,065.99
Adjusted net income.....	\$39,477.21
Less: 20 per cent of adjusted net income.....	7,895.44
Undistributed adjusted net income.....	\$31,581.77
Surtax:	
30% of \$31,581.77.....	\$ 9,474.53
Penalty of 25%, Section 406, Revenue Act of 1935,...	2,368.63
Deficiency of personal holding company surtax and penalty,	\$11,843.16

ADJUSTMENT TO NET INCOME.

Taxable year ended December 31, 1936.

Net income as disclosed by return on Form 1120,....	\$111,460.51
Additional deduction:	
Accrued capital stock tax.....	71.00
Net income adjusted,.....	\$111,389.51

EXPLANATION OF ADJUSTMENTS.

The allowable deduction for Federal Capital Stock tax is represented by the amount of \$1,821.00 for the year ended June 30, 1937 which accrued and became a liability on July 1, 1936, in lieu of the amount of \$1,750.00 paid in the taxable year and claimed as a deduction from income.

It is held that for the taxable year you were a personal holding company as defined in Section 351(b) (1) of the Revenue Act of 1936, and are subject to the surtax imposed by Section 351(a) of such Revenue Act.

Since you failed to file a personal holding company return as required by Section 351(c) of the Revenue Act of 1936, the imposition of the 25% penalty imposed by Section 291 of such Revenue Act is mandatory.

COMPUTATION OF TAX.

Taxable year ended December 31, 1936.

NORMAL INCOME TAX.

Taxable net income,.....	\$111,389.51
Less: Excess-profits tax,	None
Normal-tax net income,.....	\$111,389.51

Normal tax:

8% of \$ 2,000.00.....	\$ 160.00
11% of \$13,000.00.....	1,430.00
13% of \$25,000.00.....	3,250.00
15% of \$71,389.51.....	10,708.43

Total normal tax,.....\$15,548.43

SURTAX ON UNDISTRIBUTED PROFITS.

Section 14.

Taxable net income.....	\$111,389.51
Less: Normal tax.....	15,548.43
Adjusted net income.....	\$ 95,841.08
Dividends paid credit.....	40,000.00
Undistributed net income.....	\$ 55,841.08
Surtax:	
7% of \$ 9,584.10.....	\$ 670.89
12% of 9,584.11.....	1,150.09
17% of 19,168.22.....	3,258.60
22% of 17,504.65.....	3,851.02
Total surtax.....	\$ 8,930.60
Normal tax.....	15,548.43
Total income tax (normal tax and surtax).....	\$ 24,479.03
Income tax assessed (normal tax and surtax):	
Original, account No. 404177.....	24,500.85
Overassessment of income tax.....	\$ 21.82

PERSONAL HOLDING COMPANY SURTAX.

Section 351.

Taxable net income.....	\$111,389.51
Less: Federal income taxes.....	24,479.03
Adjusted net income.....	\$ 86,910.48
Less: 20% of adjusted net income.....	\$17,382.10
Dividends paid credit.....	40,000.00
Undistributed Adjusted net income.....	\$ 29,528.38

Surtax:

8% of \$ 2,000.00.....	\$ 160.00
18% of 27,528.38.....	4,955.11
<hr/>	
Total surtax, Section 351,.....	\$ 5,115.11
Penalty of 25%, Section 291,.....	1,278.78
<hr/>	
Deficiency of personal holding company surtax and penalty,.....	\$ 6,393.89
	[33]

ADJUSTMENTS TO NET INCOME.

Taxable year ended December 31, 1937.

Net income as disclosed by return on Form 1120,	\$119,432.24
Unallowable deductions:	
(a) Capital stock tax for year ended June 30, 1937,	\$1,821.00
(b) Capital stock tax for year ended June 30, 1938,	1,870.00 3,691.00
<hr/>	
Net income, adjusted,.....	\$123,123.24

EXPLANATION OF ADJUSTMENTS.

(a) Federal capital stock tax of \$1,821.00 for the year ended June 30, 1937, deduction for which was claimed in the return, accrued and became a liability on July 1, 1936 and the deduction was allowed for the taxable year ended December 31, 1936.

(b) Federal capital stock tax for the year ended June 30, 1938, which you accrued as a liability and deducted in your return in an amount of \$1,870.00, is not an allowable deduction from income for the taxable year for the reason that a capital stock tax return was filed for the said year making a new

- declaration of "no value" for your capital stock (as permitted by the Revenue Act of 1938), and the Lane-Wells Company gave no effect to any liability assumed for such capital stock tax.

It is held that for the taxable year you were a personal holding company as defined in Section 351 of the Revenue Act of 1936 (Title 1A) as amended by Section 1 of the Revenue Act of 1937, and are subject to the surtax imposed by Section 351 of such amended Revenue Act.

Since you failed to file a personal holding company return as required by Section 358 of such amended Revenue Act, the imposition of the 25% penalty imposed by Section 291 is mandatory.

The return filed for the taxable year purports to account for the taxable income for the period from January 1 to August 31, 1937; after which latter date the business of your corporation was taken over and its activities conducted by Lane-Wells Company, pursuant to an agreement for reorganization entered into on or about June 1, 1937. [34]

The contention made in your protest, that the said return erroneously accounted for income accruing after June 1, 1937 which should have been returned by the successor corporation, is denied for the reason that the transfer of your assets and business was not effected at the time indicated in your protest and the items of income and deduction involved were properly reflected in your books and return.

The further contention raised in your protest, that

you should be allowed a further dividends paid credit (not claimed in your return) on account of assets distributed in complete liquidation, is denied for the reason that Article 27(f)—1 of Regulations 94 provides that no such credit is allowable in respect of non-taxable distributions.

COMPUTATION OF TAX.

Taxable year ended December 31, 1937.

NORMAL INCOME TAX.

Taxable net income,.....	\$123,123.24
Less: Excess-profits tax,.....	None
Normal-tax net income,.....	\$123,123.24
Normal tax:	
8% of \$ 2,000.00.....	\$ 160.00
11% of 13,000.00.....	1,430.00
13% of 25,000.00.....	3,250.00
15% of 83,123.24.....	12,468.49
Total normal tax,	\$17,308.49

[35]

SURTAX ON UNDISTRIBUTED PROFITS.

Taxable net income,.....	\$123,123.24
Less: Normal tax,	17,308.49
Adjusted net income,	\$105,814.75
Less: Dividends paid credit,	40,000.00
Undistributed net income,	\$ 65,814.75

Surtax:

7% of \$10,581.48.....	\$ 740.70
12% of 10,581.48.....	1,269.78
17% of 21,162.95.....	3,597.70
22% of 21,162.95.....	4,655.85
27% of 2,325.89.....	627.99

Total surtax,\$10,892.02

Normal tax,17,308.49

Total income tax (normal tax and surtax),

\$ 28,200.51

Income tax assessed (normal tax and surtax):

Original, account No. 404456.....

27,003.71

Deficiency of income tax,

\$ 1,196.80

PERSONAL HOLDING COMPANY SURTAX.

Taxable net income,

\$123,123.24

Less: Federal income taxes,

28,200.51

Adjusted net income,

\$ 94,922.73

Less: Dividends paid credit,

40,000.00

Undistributed adjusted net income,

\$ 54,922.73

Surtax:

65% of \$ 2,000.00.....	\$ 1,300.00
75% of 52,722.73.....	39,692.05

Total personal holding company surtax,

\$ 40,992.05

Penalty of 25%, Section 291.....

10,248.01

Deficiency of personal holding company surtax and penalty,

\$ 51,240.06

[Endorsed]: U.S.B.T.A. Filed Aug. 22, 1939. [36]

[Title of Board and Cause—Docket No. 99830]

ANSWER

Comes now the respondent by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed in the above-entitled proceeding, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the petition.
2. Admits the allegations contained in paragraph 2 of the petition.
3. Admits that the taxes in controversy are income taxes for the year 1937, personal holding company surtax for the years 1934 to 1937, inclusive, and a 25% penalty on personal holding company surtaxes for the years 1934 to 1937, inclusive.
4. (a) to (k), inclusive. Denies the allegations of error set forth in subparagraphs (a) to (k), inclusive, of paragraph 4 of the petition. [37]
5. (a) to (n), inclusive. Denies the allegations of fact contained in subparagraphs (a) to (n), inclusive, of paragraph 5 of the petition.
6. Denies generally and specifically each and every allegation contained in the petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the petition be de-

nied and that the respondent's determination be in all respects approved.

(Signed) J. P. WENCHEL

FTH

J. P. WENCHEL,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

ALVA C. BAIRD,

FRANK T. HORNER,

E. A. TONJES,

Special Attorneys,

Bureau of Internal Revenue.

EAT:E 10/12/39

[Endorsed]: U.S.B.T.A. Filed Oct. 18, 1939. [38]

[Title of Board and Cause.]

Docket Nos. 99829, 99830. Promulgated January 31, 1941.

FINDINGS OF FACT AND OPINION

1. Amounts constituting 15 percent of the gross receipts of certain corporations from gun perforation of oil wells received by the taxpayer corporation, more than 50 percent of whose stock was owned by not more than 5 individuals, in return for the use of from 85 to 100 of the taxpayer's patents and applications, of which 7 or 8 patents

related to gun perforation, held to be "royalties" within section 351 (b) (1) of the Revenue Acts of 1934 and 1936 and section 353 of the Revenue Act of 1936, as amended by section 1 of the Revenue Act of 1937, and the taxpayer corporation held to be a "personal holding company" within section 351 (b) (1) of the Revenue Acts of 1934 and 1936 and section 352 (a) of the Revenue Act of 1936, as amended, and subject to surtax under section 351 (a) of the Revenue Acts of 1934 and 1936 and section 351 of the Revenue Act of 1936, as amended.

2. The four stockholders of the taxpayer corporation, more than 80 percent of whose gross income was personal holding company income within section 353 of the Revenue Act of 1936, as amended by section 1 of the Revenue Act of 1937, signed a reorganization agreement in the first half of the taxable year, whereby a new corporation to be formed was to issue its stock in exchange for the stock of several corporations owned by the four stockholders of the taxpayer. During the last half of the year the new corporation secured a permit authorizing it to issue its stock and issued the stock and the taxpayer corporation transferred its assets to the new corporation and filed a certificate of winding up and dissolution. Held, the requirement that "at any time during the last half of the taxable year" more than 50 percent of the taxpayer's stock be owned by not more than five individuals had been met and the taxpayer was a "per-

sonal holding company" within section 352 (a) of the Revenue Act of 1936, as amended.

3. A personal holding company which distributed in liquidation, pursuant to a tax-free reorganization under section 112 (b) (6) of the Revenue Act of 1936, amounts representing earned surplus chargeable to earnings and profits accumulated subsequent to [39] February 28, 1913, held, entitled to a dividends paid credit for such amounts under section 27 (f) of the Revenue Act of 1936 without limitation by subsection (h) in determining its surtax on undistributed profits and its personal holding company surtax for 1937. Credit Alliance Corporation, 42 B. T. A. 1020, followed.

4. Petitioner Technicraft Engineering Corporation filed its income and excess profits tax returns for 1934 and 1935 on Form 1120 within the time required by law. The taxpayer, in good faith, believed that it was not a personal holding company and filed no return as a personal holding company on Form 1120 H, as required by law and Treasury regulations. Taxpayer's income and excess profits tax returns filed on Form 1120 made a full disclosure of its gross income and deductions and its resulting net income. Held, since the taxpayer failed to file a return as a personal holding company on Form 1120 H as required by law and Treasury regulations, the period of limitations prescribed by section 275 (a), Revenue Act of 1934,

has not run so as to bar the assessment of deficiencies in personal holding company surtaxes for the years 1934 and 1935.

5. A personal holding company filed income and excess profits tax returns for 1934, 1935, 1936, and 1937 on Form 1120 within the time required by law, in which a full disclosure was made of its gross income and deductions and resulting net income, but failed to file personal holding company returns on Form 1120 H for those years. Held, the imposition of 25 per cent delinquency penalties is mandatory under the applicable revenue acts and the Treasury regulations promulgated in pursuance thereof.

Raphael Dechter, Esq., for the petitioners.

E. A. Tojnes, Esq., and Alva C. Baird, Esq., for the respondent.

The Commissioner determined deficiencies in personal holding company surtax and penalties for the years 1934, 1935, 1936, and 1937 against the Technicraft Engineering Corporation, and against the Lane-Wells Co., as transferee, as follows:

	Surtax	Penalty
1934	\$ 3,178.80	\$ 794.70
1935	9,474.53	2,368.63
1936	5,115.11	1,278.78
1937	40,992.05	10,248.01

The Commissioner also determined an overassessment of \$21.82 in income tax for 1936 and a deficiency of \$1,196.80 in income tax for 1937 of the Technicraft Engineering Corporation and Lane-Wells Co., as transferee.

The petitions of the petitioners assign errors as follows:

(a) The Commissioner erred in determining that petitioner was a "personal holding company" for each of the years 1934 to 1937 inclusive. [40]

(b) The Commissioner erred in failing to determine that the amounts of petitioner's income designated "royalties" were in fact compensation for tangible services rendered to affiliated corporations and as such did not constitute "personal holding company" income.

(c) The Commissioner erred in determining that the failure of petitioner to file Form 1120-H for each of the years 1934 to 1937 inclusive was not due to reasonable cause.

(d) The Commissioner erred in asserting penalties of 25% of the surtax on personal holding companies for delinquency in filing Form 1120-H for each of the years 1934 to 1937 inclusive.

(e) The Commissioner erred in failing to determine that the period for assessment of any deficiency or penalty in respect of the 1934 income of petitioner had expired prior to the issuance of the deficiency notice.

(f) The Commissioner erred in failing to determine that the period for assessment of any deficiency or penalty in respect of the 1935 income of petitioner had expired prior to the issuance of the deficiency notice.

(g) In determining the liability of petitioner for surtax on undistributed profits and for surtax on personal holding companies in respect of its 1937 income, the Commissioner erred in not allow-

ing a "dividends paid credit" for amounts distributed during 1937 in final and complete liquidation of petitioner.

(h) The Commissioner erred in failing to determine that there was an overassessment of surtax on undistributed profits against petitioner for 1937 of \$10,248.87.

(i) The Commissioner erred in failing to determine that the income and deductions reported by petitioner [Technicraft Engineering Corporation] for the period from June 1, 1937 to August 31, 1937, in fact constituted income and deductions of Lane-Wells Company, the successor corporation and not income and deductions of petitioner.

(j) The Commissioner erred in failing to determine that there was an overassessment of normal income tax against petitioner for 1937 of \$7,483.16.

(k) The Commissioner erred in failing to recognize that by his past acts and conduct he is estopped from asserting any claim of liability against petitioner for surtax on personal holding companies or penalties thereon.

FINDINGS OF FACT

Petitioner Technicraft Engineering Corporation, hereinafter called Technicraft, a California corporation with its principal office in Los Angeles, was organized in December 1932, but remained inactive until March 1, 1934. Petitioner Lane-Wells Co., a Delaware corporation with its principal office in Los Angeles, was organized in 1937.

The Lane-Wells Co., a California corporation, hereinafter called Lane-Wells Co. of California, was organized in March 1932. In that year it began selling packers, swabs, and swab rubbers as merchandise and sought to find new products that could be sold in the oil industry as merchandise or in the form of service. In June 1932 it began work on a gun perforator to be used in oil fields and organized Technicraft for the purpose of doing engineering and experimental research. On December 21, 1932, the Lane-Wells Co. of California obtained from Sidney W. Mims, under an exclusive [41] license agreement, an exclusive license to use and sell devices embodying an invention for perforating well casing for which Patent No. 1,582,184, dated April 27, 1926, had been issued to Mims. Under the agreement the Lane-Wells Co. of California was to pay \$100 per month until March 1, 1934, and \$200 per month thereafter. On March 1, 1934, the Lane-Wells Co. of California executed an assignment of exclusive license agreement, transferring to Technicraft its right to the exclusive license. On the same date Technicraft executed a sublicense agreement granting to the Lane-Wells Co. of California, "in consideration of the royalty hereinafter provided", a sublicense restricted to the State of California and including "any and all rights, privileges and remedies which it [Technicraft] might or could do, exercise or perform" under the assignment of exclusive license agreement. The sublicense agreement further provided, in part:

In consideration of the granting of said sub-license, said Lane-Wells Co., as sub-licensee, does hereby agree to pay to the Technicraft Engineering Corporation, a sub-licensor, a royalty of fifteen (15%) per cent of any and all gross receipts derived from the manufacture, sale, rental or use of any device of any kind by virtue of this sub-license agreement, such royalty to be payable on the 20th day of each and every month for the royalties accruing for the month previous. * * *

On February 13, 1936, Technicraft executed a license agreement granting to the Lane-Wells Co. of Oklahoma, an Oklahoma corporation, having a place of business at Oklahoma City, Oklahoma:

* * * a non-exclusive license in and throughout the States of Oklahoma, Kansas, Wyoming, Colorado, and Montana only, subject to the terms and conditions of this agreement, to make or purchase for the Licensee's own use only, and to use but not to sell, rent, or lease to others said Perforators.

The license agreement also provides, in part:

I. Definitions:

The term "Perforators" shall be construed to mean not only the patent specifically mentioned hereinbefore, but also any and all inventions, applications, patents and any continuations, divisions, and/or reissues thereof and whether in the nature of apparatus or processes.

which the Licensor now owns or controls or which it may at any time during the life of this agreement own or control and which relate or are accessories to said Perforators. The term "Patent Rights" shall be construed to embrace as a group all the patents and applications herein specified or referred to or implied. The term "gross receipts" shall be construed to mean the total receipts derived in any manner whatsoever from the manufacture and/or use of any and all apparatus or processes covered by said Patent Rights without deductions of any kind or character.

* * * * *

IV. Royalties:

The royalty payments on the Patent Rights herein licensed shall be fifteen percent (15%) of the gross receipts; minimum royalties shall be not less than Seven Hundred and Fifty Dollars (\$750.00) per month.

* * * * *

[42]

VII. Improvements by Licensee:

Licensee shall disclose to Licensor all inventions, applications, patents, or continuations, divisions and/or reissues, dominated by the Patent Rights Herein Defined which the Licensee may now own or control during the life of this agreement, or which may be jointly or solely invented by any officer, executive, agent, or employee of the Licensee; it being understood that the Licensee shall, upon execution of

this agreement, enter into the necessary agreements with its officers, executives, agents and employees to give effect to this section.

Under disclosure of such inventions, applications, patents, or continuations, divisions and/or reissues, dominated by the patent rights, the Licensor shall have a forty-five (45) day option period to accept and incorporate the same with the patent rights herein licensed; and, if the nature of the subject matter so accepted requires, to file the necessary patent applications thereon at its own expense. Should the Licensor fail to exercise its option, the Licensee shall retain full rights thereto.

On the same date Technicraft executed a similar agreement granting to the Lane-Wells Co. of Texas, a Texas corporation having a place of business at Houston, Texas, a "non-exclusive license in and throughout the States of Texas, Louisiana, Mississippi, Arkansas and New Mexico." The Texas corporation had been engaged in the business of gun perforating since September or October 1935. The Lane-Wells Co. of California, the Lane-Wells Co. of Texas, and the Lane-Wells Co. of Oklahoma each did a merchandise and oil field service business in their respective areas of operation. The business included the operation of a gun perforator, a strata-graph, which recorded by electricity the various formations underground, a fishing magnet, and fishing tools.

Technicraft conducted experiments, purchased

test instruments, and built models of devices, some of which were sold to the Lane-Wells Co. of California. Lane and Wells and employees of Technicraft assigned more than 50 patents to Technicraft. Technicraft owned at least 19 abandoned and unfiled inventions and in 1937 it had from 85 to 100 patents or patent applications which it was furnishing to the Lane-Wells companies on June 1, 1937, and of which 7 or 8 related to the basic principle of the Mims patent.

The purpose of the gun perforator is to make holes in pipe underground by shooting bullets horizontally through the casing and formations back of the casing after the gun has been lowered into a well by means of an electric cable which is operated from a truck with a pulley and hoist. At first the gun was used to perforate oil sands that had formerly been considered not worth while but many new uses for the gun have since been developed. The method enables perforation anywhere in the well.

Technicraft developed the type of truck used in the gun perforation business. It permits use of the truck motor for hoisting. [43] Technicraft also developed a brake for lowering the cable, a control panel, a throttle, an armature to indicate speed, a weight indicator, bridging plugs, pumping units, a fishing magnet, a device for measuring cable, a loud speaker for voice communication between the truck and the derrick floor of the well, a packing gland, which was a safety device to prevent the es-

cape of gas or oil, a method of using an X-ray machine on cable to determine deterioration, and safety switches to prevent accidental firing of the gun. A strata-graph developed by Technicraft from November 1935 through the middle of 1937 at an expense of between \$50,000 and \$60,000 was sold to the Lane-Wells companies but was finally abandoned, since it had no advantages over known geology. The various Lane-Wells companies did not have research or engineering departments but left all research to Technicraft. Technicraft sold apparatus to the various Lane-Wells companies at cost plus a slight profit. These sales of apparatus were never in any large amount in any taxable year. As the Lane-Wells companies developed manufacturing facilities, they took over manufacture. The merchandise sales were included on Technicraft's return as royalties. The amounts so included were small and the exact amounts are not given separately in the returns. In 1936 Technicraft occupied a building which was designed for it and contained electric and chemical laboratories, offices for engineers, and an X-ray room.

It would not have been possible to conduct a successful gun perforation business with the Mims patent alone, since it was merely a basic patent covering the idea of lowering a gun into a well and shooting a bullet horizontally to perforate the casing and made no provision for withstanding the explosion, for sealing the powder, and for satisfactorily lowering and raising the gun. Technicraft

developed a method of delayed fire, of sealing the gun, and a cable for lowering and raising the gun. The cable contained in its center a copper line for conveying electricity. These improvements by Technicraft made the gun perforator far more serviceable and valuable than was the gun perforator covered by the original Mims patent.

When the original exclusive license agreement was made with Mims by the Lane-Wells Co. of California on December 21, 1932, Lane and Wells agreed between themselves to set aside 15 percent of the income of the Lane-Wells Co. of California for research and development. No additional charge was made aside from the 15 percent of gross receipts provided for in the sublicense agreement with the Lane-Wells Co. of California and the license agreements with the Lane-Wells Co. of Texas and the Lane-Wells Co. of Oklahoma, although improvements were made by Technicraft on packers assigned to it by the Lane-Wells Co. of California. There was no license agreement between [44] Technicraft and Lane-Wells International Inc., a California corporation operating in foreign countries, but Technicraft collected 15 percent of the gross receipts of Lane-Wells International, Inc., from gun perforation, as it did from the other Lane-Wells companies. The license agreements of Technicraft with the Lane-Wells Co. of Texas and the Lane-Wells Co. of Oklahoma expired in February 1937, and although no new agreements were executed those companies continued to pay 15 percent

of their gross receipts from gun perforation to Technicraft until it was merged with the Lane-Wells Co. of Delaware.

Throughout the time during which Technicraft was doing business all of its stock and all of the stock of the Lane-Wells Co. of California was owned by W. G. Lane, W. T. Wells, and their wives. They also owned all of the stock of the Lane-Wells Co. of Oklahoma, the Lane-Wells Co. of Texas, and Lane-Wells International, Inc., and Alexander Anderson, Inc., a California corporation. Lane and Wells were directors and officers of the various companies.

In 1936 Lane and Wells discussed with an attorney, a broker, and an accountant a proposed reorganization of Technicraft and the various Lane-Wells companies into a new corporation, to be known as the "Lane-Wells Company", a Delaware corporation, and on June 1, 1937, a reorganization agreement was signed by Lane and Wells and their wives and by officers of Technicraft, the various Lane-Wells companies, including the new Delaware corporation, and Alexander Anderson, Inc. The reorganization agreement provided in part:

First: It is hereby stated and agreed that the stockholders shall surrender all of their stock in each and all of the constituent companies to the Delaware company in exchange for such proportionate share of an issue of 250,000 shares of the Delaware company, the receipt of which will leave said stockholders

and each of them in proportionately and substantially the same position with reference to the Delaware company as is now held by each and all of them in the various constituent companies.

Second: It is hereby agreed and stated that the Delaware company shall forthwith secure the necessary legal permission to issue 250,000 shares of its authorized capital of 500,000 shares of no par value stock for the purpose of transferring and exchanging the same for all the stock in the various constituent companies, such exchange of stock to take place upon such legal permission being secured.

Third: It is understood and agreed that the amount of stock of the Delaware company that is to be received by each of the stockholders is to be determined by the proportion of the value of the stock of each of the stockholders to the aggregate value of all of the stock of the constituent companies. It is intended that by the term "value" hereinafter and hereinbefore used, shall be meant the book value of the stock of each of the companies as of the date of June 1st, 1937, and which book value shall be determined by a certified public accountant from the books of the constituent companies.

On July 22, 1937, a permit was granted by the State Corporation Department of California authorizing the new Delaware corporation [45] to

issue 250,000 shares of stock to Wells and Lane and their wives in consideration for the transfer of all of the stock of the various Lane-Wells companies. The stock was actually issued by the new Delaware corporation to Wells and Lane and their wives in equal proportions on July 29, 1937. Technicraft, on July 29, 1937, issued its certificate No. 7 for 25,000 shares of stock, being all of its issued and outstanding capital stock, to the new Delaware corporation. The certificate was based upon the reissuance of the certificates formerly held by Wells and Lane and their wives.

Immediately after the execution of the reorganization agreement negotiations were entered into with brokers for the sale of 60,000 shares of stock of the new corporation to the public and in August 1937 an agreement with the brokers was made under which the brokers, as agents, offered to the public in October 1937 and later sold 60,000 shares.

In July 1937 the president and the secretary of Technicraft executed two separate assignments of Technicraft's assets to the new corporation. Technicraft's board of directors, by a resolution on August 27, 1937, directed the transfer of its assets. The assets were actually transferred at various times when the necessary documents were filed and recorded. On Technicraft's books the transfer of all the assets was recorded as of August 31, 1937. Technicraft's books in 1937 showed net profits for the months through August, before adjustments for taxes, as follows:

Five months ended May 31.....	\$ 65,270.52
June	16,861.44
July	16,873.36
August	13,598.76
Total.....	112,604.08

In 1937 Technicraft's balance sheets at the end of each month from May through August showed total assets in excess of total liabilities as follows:

May 31	\$135,052.52
June 30	151,913.96
July 31	168,787.32
August 31	155,660.84

On October 22, 1937, a certificate of winding up and dissolution of Technicraft, stating that the corporation had been completely wound up, that all of its known assets had been distributed, and that taxes and all other known debts and liabilities had been paid or provided for, was filed by its directors with the Secretary of State of the State of California.

Technicraft filed its corporation income and excess profits tax returns on Form 1120 for 1934 on or about March 15, 1935; for 1935, [46] on or about March 15, 1936; for 1936, on or about March 15, 1937; and for 1937, on or about March 15, 1938.

Technicraft's return for 1934 reported gross income from royalties of \$27,125.23 and total deductions of \$11,392.24, leaving a net income of \$15,732.99. Its return for 1935 reported "gross profits where inventories are not an income determining factor", \$69,577.19, and discounts, \$13.90, making

a total gross income of \$69,591.09. Total deductions were taken on the return of \$21,562.89, leaving net income of \$48,028.20. Its return for 1936 reported gross income from interest, \$822.01; rents, \$2,500; and from royalties, \$145,113.73; discounts, \$92.08, making a total gross income of \$148,527.82. From this gross income, total deductions of \$37,067.31 were taken, leaving net income of \$111,460.51. Its return for the year 1937, covering the period from January 1 to August 31, 1937, showed gross income from interest, \$225.98; rents, \$8,000; royalties, \$157,932.24; and discounts \$42.19, making gross income of \$166,200.41. From this gross income, deductions were taken of \$46,768.17, leaving net income of \$119,432.24.

Technicraft, in its return for 1934, stated it was in the engineering business; in its 1935 return stated its business was "engineering development"; in its 1936 return stated its business was "research and engineering"; and on its 1937 return stated its business was "research and engineering."

Technicraft did not file personal holding surtax returns on Form 1120 H for either 1934, 1935, 1936, or 1937.

Technicraft's income tax returns were prepared by its accountant or his assistants and were signed by Wells as president and by Technicraft's secretary. The accountant, in addition to his work as a certified public accountant, also engaged in tax work and gave Technicraft his opinion that it was not a personal holding company. He had confer-

ences with representatives of the Bureau of Internal Revenue and gave them access to Technicraft's books and records. On June 19, 1937, Technicraft received a refund of \$278.37 in respect of income and excess profits taxes paid by it for 1935 and at that time the Commissioner made no claim that Technicraft was a personal holding company.

It is stipulated that petitioner Lane-Wells Co. is liable as a transferee for any taxes which may be found to be due from Technicraft.

OPINION.

Black:

Issues (a) and (b).—These two assignments of error raise essentially the same issue, which is that the Commissioner erred in his determination in the notice of deficiency that Technicraft was [47] a "personal holding company" as defined in section 351 (b) (1) of the Revenue Acts of 1934 and 1936, and section 352 (a) of the Revenue Act of 1936 as amended by section 1 of the Revenue Act of 1937.

Sec. 351. Surtax on Personal Holding Companies.

(b) Definitions.—As used in this title—
 (1) The term "personal holding company" means any corporation * * * if—(A) at least 80 per centum of its gross income for the taxable year is derived from royalties, * * * and (B) at any time during the last half of the taxable year more than 50 per centum in value of its outstanding stock is owned, directly or indirectly, by or for not more than five individuals. * * *

Sec. 352. Definition of Personal Holding Company.

(a) General Rule.—For the purposes of this

and that it was subject to the surtax imposed by section 351 (a) of the Revenue Act of 1934 and 1936 and by section 351 of the Revenue Act of 1936 as amended. Petitioners contend that the amounts of Technicraft's income designated on its income tax returns as "royalties" were in fact compensation for tangible services rendered to affiliated corporations and did not constitute "personal holding company" income.

All of the license agreements in evidence apply to the term "royalty" to the amounts paid to Technicraft thereunder, although the terms of the licenses vary as to the exact nature of the consideration for which the payments were made. Technicraft granted to the Lane-Wells Co. of California merely "any and all rights, privileges and remedies" which Technicraft "might or could do, exercise or perform" under the assignment of the exclusive license to use and sell devices, embodying the Mims patent, but it is quite clear from the language of the other two license agreements that the "royalty payments" thereunder were not confined to receipts from the use of the Mims patent alone.

title and of Title I the term "personal holding company" means any corporation if—

(1) **Gross Income Requirement.**—At least 80 per centum of its gross income for the taxable year is personal holding company income as defined in section 353; * * *

(2) **Stock Ownership Requirement.**—At any time during the last half of the taxable year more than 50 per centum in value of its outstanding stock is owned, directly or indirectly, by or for not more than five individuals.

Under each of the license agreements with the Lane-Wells Co. of Oklahoma and the Lane-Wells Co. of Texas, Technicraft granted a nonexclusive license "to make or purchase for the Licensee's own use only, and to use but not to sell, rent, or lease to others said Perforators." In those agreements the term "perforators" was broadly defined "to mean not only the patent specifically mentioned hereinbefore, but also any and all inventions, applications, patents and any continuations, divisions, and or reissues thereof and whether in the nature of apparatus or processes which the licensor now owns or controls or which it may at any time during the life of this agreement own or control and which [48] relate or are accessories to said Perforators." The agreements provided that "The royalty payments on the Patent Rights herein licensed shall be fifteen percent (15%) of the gross receipts; minimum royalties shall be not less than Seven Hundred and Fifty dollars (\$750.00) per month", that "The term 'Patent Rights' shall be construed to embrace as a group all the patents and applications herein specified or referred to or implied", and that "The term 'gross receipts' shall be construed to mean the total receipts derived in any manner whatsoever from the manufacture and/or use of any and all apparatus or processes covered by said Patent Rights without deductions of any kind or character."

Under the license agreements with the Lane-Wells Co. of Texas and the Lane-Wells Co. of Oklahoma, Technicraft was the grantor of the pat-

ents and applications used by the Lane-Wells companies. The payments received by it were proportionate to the use of the patents and applications, since the payments were 15 percent of the gross receipts from any and all inventions, applications, and patents which related or were accessories to the perforators. The payments thus fall clearly within the definition of "royalty" given in Black's Law Dictionary, 3d. ed., as "A payment reserved by the grantor of a patent, lease of a mine, or similar right, and payable proportionately to the use made of the right by the grantee." This definition is well supported by authority. *Western Union Telegraph Co. v. American Bell Telephone Co.*, 125 Fed. 342; *In re Elsner's Will*, 206 N. Y. S. 765; *Bellport v. Harrison*, 123 Kans. 310; 255 Pac. 529; *Volk v. Volk Manufacturing Co.*, 101 Conn. 594; 126 Atl. 847; *Kiesau Petroleum Corporation*, 42 B. T. A. 69.

It seems clear that some of the payments made to Technicraft were not covered by express license agreements. For example, Technicraft had no license agreement at all with Lane-Wells International, Inc., although it collected 15 percent of that corporation's gross receipts from gun perforation. In February 1937 Technicraft's agreements with the Lane-Wells Co. of Texas and the Lane-Wells Co. of Oklahoma expired, but those corporations continued to pay to Technicraft 15 percent of their gross receipts from gun perforation. The facts further show that on June 4, 1937, Technicraft was

furnishing the Lane-Wells companies with from 85 to 100 patents or patent applications, of which only 7 or 8 related to the basic principle of the Mims patent.

In their argument that the payments in question did not constitute royalties, petitioners rely on *Kiesau Petroleum Corporation, supra*, wherein a certain percentage of the proceeds from the sale of oil received by a taxpayer, under contracts with lessees of oil producing [49] land in return for equipment was held not "derived from royalties" within the meaning of section 351(b) (1) of the Revenue Acts of 1934 and 1936 and the taxpayer was held not to be a personal holding company. The Board held that under the contracts the taxpayer "did not reserve an interest in the oil producing properties; it acquired such an interest for the first time." The instant case is clearly distinguishable, since *Technicraft* had an interest in patents and applications and under the license agreements "reserved" an interest rather than "acquiring" it for the first time, and in those cases where there were no license agreements it seems clear that the nature of the income was the same.

Petitioners also rely upon *Affiliated Enterprises, Inc.*, 42 B. T. A. 390, wherein the taxpayer operated a sales promotion plan, known as "bank night", which was not and could not be patented or copyrighted, except for some instruction sheets which were copyrighted. The taxpayer provided a few simple articles to execute the idea, derived

income in the form of a flat sum weekly payment from "license agreements" with theatre operators, and was held not to be a personal holding company, since its income was not derived from royalties. The case is distinguishable in that Technicraft owned patents and applications, many of which were patentable, and received not a flat sum, but 15 percent of the gross receipts derived by each Lane-Wells company from the use of such patents and applications in gun perforation. Moreover, it has been held that the term "royalty" may be applied to receipts derived in respect of nonpatentable improvements. *Volk v. Volk Manufacturing Co.*, *supra*.

Petitioners have not shown what portion of Technicraft's income, if any, was derived from engineering services or from nonpatentable devices, as distinguished from patents, and they have not shown the amounts derived under the written license agreements, as distinguished from the amounts received from Lane-Wells International, Inc., and from the Lane-Wells Co. of Texas and the Lane-Wells Co. of Oklahoma after the written license agreements had expired in February 1937. Although Technicraft furnished the Lane-Wells companies with from 85 to 100 patents or applications, of which only 7 or 8 related to the basic principle of the Mims patent, petitioners have not shown what portion of the amounts received by Technicraft was consideration for patents related to the basic principle of the Mims patent. The facts

show that on its books for all the years involved and on its income tax returns for 1934, 1936, and 1937, Technicraft treated the payments made to it as royalties. We agree, of course, with petitioners that merely calling these receipts "royalties" in the license agreements and on petitioner's books would not make them "royalties" if, in fact, the evidence showed that they were some- [50] thing else. However, for reasons already stated, we think these payments were "royalties" within the meaning of the applicable revenue act.

These amounts did not constitute royalties merely to the extent of an amount equal to the \$200 per month paid by Technicraft for the Mims patent, as petitioners suggest, since the payments to Technicraft were not made solely for the use of the Mims patent, which by itself was not very valuable. It was the improvements and developments to the basic Mims patent, conceived and carried out by Technicraft, which made its use of great value. Manifestly the chief business purpose of Technicraft was to improve and develop the Mims patent and other patents and devices used in the oil business by the Lane-Wells companies. For the use of these patents and devices and their improvements, it received 15 percent of the gross receipts of the different Lane-Wells companies which they in turn received from the gun perforating business. These were none the less royalties, we think, even though they were not received in anything like their entirety for the use of the basic Mims patent.

Therefore, the payments received by Technicraft must be held to be "royalties" within section 351 (b) (1) of the Revenue Acts of 1934 and 1936, and, since petitioners do not contest the fact that Technicraft otherwise falls within the definition of a "personal holding company" for the taxable years 1934, 1935, and 1936, the respondent's position as to those years is sustained. *Logan Coal & Timber Association*, 42 B. T. A. 529. The payments were also "royalties" within section 353 (a) of the Revenue Act of 1936, as amended by section 1 of the Revenue Act of 1937, but an additional objection is raised by petitioners in respect of taxability for 1937.

Issues (i) and (j).—Petitioners contend that even if Technicraft be considered a personal holding company in the years 1934 through 1936, it could not have been a personal holding company in 1937 "for the reason that during the latter half of 1937, it had neither assets nor income, and 50% or more of its stock was not held by less than five individuals or their families."

Section 352.(a), of the Revenue Act of 1936, as amended by section 1 of the Revenue Act of 1937, includes in the definition of a "personal holding company" any corporation if at least 80 percent of its gross income is personal holding company income and, in addition:

At any time during the last half of the taxable year more than 50 per centum in value of its outstanding stock is owned, directly or

indirectly, by or for not more than five individuals.

The question in issue hinges upon the meaning of "at any time during the last half of the taxable year." Section 357 of the Revenue Act of 1936, as amended, provides that "The terms used in this title [51] shall have the same meaning as when used in Title I", and section 48 of Title I of the Revenue Act of 1936 provides, in part:

When used in this title—

(a) "TAXABLE YEAR.—"Taxable year" means the calendar year, or the fiscal year ending during such calendar year, upon the basis of which the net income is computed under this Part. "Taxable year" includes, in the case of a return made for a fractional part of a year under the provision of this title or under regulations prescribed by the Commissioner with the approval of the Secretary, the period for which such return is made.

Technicraft's income tax return for 1937 was filed for the period which began January 1, 1937, and ended August 31, 1937. If "the taxable year", for purposes of determining whether Technicraft falls within the definition of a "personal holding company" in section 352 (a) of the Revenue Act of 1936, as amended, is held to be the fractional part of a year from January 1, 1937, to August 31, 1937, for which the income tax return was filed, then Technicraft falls within the statutory defini-

tion of a "personal holding company", since at least as late as May 31, 1937, more than 50 percent of Technicraft's outstanding stock was owned directly, or indirectly, by or for not more than five individuals.

But no personal holding company return appears to have been filed by Technicraft and the parties in arguing this point in their briefs appear to have considered the taxable year in question as the calendar year ended December 31, 1937. The deficiency notice determined personal holding company surtax liability "for the taxable years ended * * * December 31, 1937" and, in the explanation of adjustments to net income, stated:

The return filed for the taxable year purports to account for the taxable income for the period from January 1 to August 31, 1937; after which latter date the business of your corporation was taken over and its activities conducted by Lane-Wells Company, pursuant to an agreement for reorganization entered into on or about June 1, 1937.

The contention made in your protest, that the said return erroneously accounted for income accruing after June 1, 1937 which should have been returned by the successor corporation, is denied for the reason that the transfer of your assets and business was not effected at the time indicated in your protest and the items of income and deduction involved were properly reflected in your books and return.

In Technicraft's petition the taxable year is treated as ending December 31, 1937, and petitioner alleged as a fact that its "last taxable year was the calendar year 1937."

If the entire calendar year 1937 is treated as "the taxable year" in this case, Technicraft meets the requirements for a "personal holding company" as set forth in section 352 (a), as amended, since the facts clearly show that Technicraft continued to exist as a corporation and had stock outstanding in the names of Lane and Wells [52] and their wives up until July 29, 1937. The reorganization agreement whereby the stock of Technicraft and the other corporations owned by Lane and Wells and their wives was to be transferred to the Lane-Wells Co., the Delaware corporation, in return for shares of its stock was signed June 1, 1937. It was not until July 22, 1937, however, that a permit was granted by the State Corporation Department of California authorizing the Delaware corporation to issue its stock. The actual issuance took place a week later, July 29, 1937. At that time Technicraft issued a new certificate of its shares to the Delaware corporation. Not until that date was there a reorganization. National Iron Works, 22 B. T. A. 382; A. T. Evans, 30 B. T. A. 746.

The instant case is clearly distinguishable on its facts from *Novo Trading Corporation v. Commissioner*, 113 Fed. (2d) 320, urged as an authority by petitioners, wherein liquidation of a corporation was held effected so that refunds of import

duties were not taxable to it although the certificate of dissolution which had been executed was never filed with the Secretary of State, since in that case at the time in question all the stock certificates had been canceled on the corporation's books and the corporation had completely ceased business activities.

On the facts we hold that the Commissioner did not err in his determination that petitioner was a personal holding company for the year 1937. This disposes of assignment of error (i) adversely to the contention of petitioners. It likewise disposes of assignment of error (j) adversely to petitioners because that assignment of error is based upon the same contention as is made in support of assignment of error (i).

Issues (g) and (h).—In the notice of deficiency the Commissioner stated:

The further contention raised in your protest, that you should be allowed a further dividends paid credit (not claimed in your return) on account of assets distributed in complete liquidation, is denied for the reason that Article 27 (f)-1 of Regulations 94 provides that no such credit is allowable in respect of non-taxable distributions.

Petitioners contend that, even if Technicraft could be construed to be a personal holding company, it nevertheless was entitled to a dividends paid credit for amounts distributed at the time of

its reorganization to the extent that such distribution represented earned surplus, and that of the amounts distributed in the liquidation of Technicraft not less than \$65,814.75 was properly chargeable to earnings and profits accumulated subsequent to February 28, 1913, and that it has overpaid its surtax on undistributed profits for 1937 in the sum of \$10,248.87. [53]

As we have already stated, all of Technicraft's assets were transferred in 1937 to the Lane-Wells Co. of Delaware, its sole stockholder, and both parties agree that there was a tax-free reorganization under section 112 (b) (6) of the Revenue Act of 1936. The parties agree that the question in issue depends upon whether subsection (f) of section 27 of the Revenue Act of 1936² is limited by subsection (h)³ in computing the "dividends paid credit" which is to be deducted under section 355 of the Revenue Act of 1936, as amended by sec-

²(f) Distribution in Liquidation.—In the case of amounts distributed in liquidation the part of such distribution which is properly chargeable to the earnings or profits accumulated after February 28, 1913, shall, for the purposes of computing the dividends paid credit under this section, be treated as a taxable dividend paid.

³(h) Nontaxable Distributions.—If any part of a distribution (including stock dividends and stock rights) is not a taxable dividend in the hands of such of the shareholders as are subject to taxation under this title for the period in which the distribution is made, no dividends paid credit shall be allowed with respect to such part.

tion 1 of the Revenue Act of 1937, from "adjusted net income" to determine the "undistributed adjusted net income" subject to surtax under section 351 of the Revenue Act of 1936, as amended.

In *Credit Alliance Corporation*, 42 B. T. A. 1020, the Board decided a similar question in accordance with the views of petitioners in this case and we now follow that decision. On the issue raised by these assignments of error, the Commissioner's determination was in error, but cf. *Centennial Oil Co. v. Thomas*, 109 Fed. (2d) 359; certiorari denied, 309 U. S. 690.

From petitioner's exhibit 28, introduced in evidence by agreement between the parties, *Technicraft's* earned surplus, at the time of its merger with the *Lane-Wells Co.* of Delaware, August 31, 1937, was \$55,660.84 and not \$65,814.75 as alleged in its assignment of error. The correct amount of *Technicraft's* earned surplus transferred to the *Lane-Wells Co.* of Delaware in the reorganization should be used in a recomputation under Rule 50.

Issues (e) and (f).—Petitioners in assignments of error (e) and (f) contend that the three-year period of limitations contained in section 275 (a) of the Revenue Act of 1934 has run for the years 1934 and 1935. The facts show that on March 15, 1935, and March 16, 1936, respectively, *Technicraft* filed its corporation income and excess profits tax returns on Form 1120 for the calendar years 1934 and 1935, respectively. These returns appear to be full and complete, aside from some minor adjust-

ments which the Commissioner made in his determination of the deficiencies. Technicraft answered "No." to the following question appearing on the face of both returns:

Is the corporation a personal holding company within the meaning of Section 351 of the Revenue Act of 1934?—(If so, an additional return on Form 1120H must be filed.)

[54]

Technicraft did not file any returns on Form 1120H because, in good faith, it did not believe it was a personal holding company.

The respondent's deficiency notice is dated June 1, 1939, which is over four years and two months after the 1934 return was filed on Form 1120 and over three years and two months after the 1935 return was filed on Form 1120. He contends that the statute never commenced to run, for the sole and only reason that no returns were filed on Form 1120 H, and relies upon section 276 (a) of the Revenue Act of 1934, which provides that in the case "of a failure to file a return the tax may be assessed * * * at any time."

Section 275 (a) of the Revenue Act of 1934 provides that the tax imposed by Title I "shall be assessed within three years after the return was filed * * *." Section 351 (c) provides:

(c). *Administrative Provisions.*—All provisions of law (including penalties) applicable in respect of the taxes imposed by Title I of this Act, shall insofar as not inconsistent with this section, be applicable in respect of the tax imposed by this section, except that the

provisions of section 131 of that title shall not be applicable.

Article 351-8 of Regulations 86, promulgated under the Revenue Act of 1934, in so far as is material, provides:

Art. 351-8. Return and payment of tax.—A separate return is required for the surtax imposed under Section 351. Such return shall be made on Form 1120H. * * * The same provisions of law relating to the period of limitation for assessment and collection which govern the taxes imposed by Title I also apply to the surtax imposed under Title IA. However, since the surtax imposed under Title IA is a distinct and separate tax from those imposed under Title I, the making of a return under Title I will not start the period of limitation for assessment of the surtax imposed by Title IA. If the corporation subject to section 351 fails to make a return, the tax may be assessed at any time. * * * The administrative provisions applicable to the surtax imposed by section 351 are not confined to those contained in Title I but embrace all administrative provisions of law which have any application to income taxes.

The returns filed on Form 1120 were made under Title I.

Petitioner, in support of its contention that the statute has run, relies upon Germantown Trust Co.

v. Commissioner, 309 U. S. 304. In that case a trustee in charge of a certain fund filed a return as a trust on Form 1041. After the statute had run for assessing an additional tax against the trust, the Commissioner determined that the fund was an association taxable as a corporation and that, since no return had been filed on Form 1120 as an association taxable as a corporation, as required by section 52 of the Revenue Act of 1932 and article 391 of Regulations 77, he was not barred from assessing the determined deficiency against the trustee in charge of the fund. The Supreme Court held that the return on Form 1041 was a return within the meaning of section 275 (a) of the Revenue Act of 1932, [55] and that the proposed deficiency in that case was barred by the statute of limitations. Among other things, the Court said:

The respondent's contention is that where a fiduciary, in good faith, makes what it deems the appropriate return, which discloses all of the data from which the tax, treated as one imposed upon an association (classified as a corporation under the statute), can be computed, such a return is to be deemed no return. We think this view inadmissible.

It cannot be said that the petitioner, whether treated as a corporation or not, made no return of the tax imposed by the statute. Its return may have been incomplete in that it failed to compute a tax, but this defect falls short of rendering it no return whatever.

At the conclusion of the foregoing language the Court in a footnote cited the following cases: *Zellerbach Paper Co. v. Helvering*, 293 U. S. 172; *Commissioner v. Stetson & Ellison Co.*, 43 Fed. (2d) 553; *United States v. Tillinghast*, 69 Fed. (2d) 718; *Abraham Werbelovsky*, 8 B. T. A. 442; *F. M. Stearns*, 16 B. T. A. 889; *J. R. Brewer*, 17 B. T. A. 704.

We think the instant case is distinguishable from the *Germantown Trust Co.* case, *supra*. In that case both the returns on Form 1041 and 1120 dealt with in the opinion were what might be properly termed Title I returns. The tax involved was a Title I income tax. In the instant case the tax involved is a Title IA tax. Treasury Regulations 86, article 351-8, above quoted, states:

* * * However, since the surtax imposed under Title IA is a distinct and separate tax from those imposed under Title I, the making of a return under Title I will not start the period of limitation for assessment of the surtax imposed under Title IA.

Is the above regulation a valid one? We think it is. In *Blenheim Co., Ltd.*, 42 B. T. A. 1248, we held that the taxpayer was liable for a delinquency penalty of 25 percent in income tax deficiency for failure to file a return on Form 1120 for the normal income tax, although it had filed a return on Form 1120 H as a personal holding company. In that case, among other things, we said: "Clearly,

the normal and surtax here in dispute are separate and distinct taxes. Revenue Act of 1934, Title I, Title I-A * * *."

In Will County Title Co., 38 B. T. A. 1396, the Commissioner determined a deficiency in income tax for 1934 and an overassessment of excess profits tax greater than the amount of the deficiency in income tax, thus making a net overassessment of the two taxes. On these facts we held that the petition for redetermination was within our jurisdiction in so far as it pertained to the deficiency in income tax, but not as to the overassessment in excess profits tax. We based our decision upon the fact that "the two taxes are imposed by entirely separate provisions of the statute", the income tax by Title I and the [56] excess profits tax by Title V, and are separate and distinct taxes. To the same effect is *Hobbs Western Co.*, 43 B. T. A. 5.

If the question of our jurisdiction is determined under certain circumstances by the character of the tax, then it is difficult to see how a return filed on Form 1120 under Title I of the Revenue Act of 1934 would start the running of the statute of limitations as to a separate and distinct tax imposed by Title IA of the Revenue Act of 1934, where no return has been filed by the taxpayer on Form 1120 H, as required by the Treasury regulations. The two returns are quite different, as pointed out by us in *Blenheim Co., Ltd.*, *supra*.

We, therefore, hold that, since *Technicraft* did not file personal holding company returns on Form

1120 H, the statute of limitations has not run and the deficiencies in personal holding company surtax for the years 1934 and 1935 are not barred by the statute of limitations.

Issues (c) and (d).—In the notice of deficiency the Commissioner added a 25 percent penalty for each year as “mandatory” under section 291 of the Revenue Act of 1934, section 406 of the Revenue Act of 1935, and section 291 of the Revenue Act of 1936, for failure to file a personal holding company return.

Petitioners contend that this was error and that, although no personal holding company returns were filed on Form 1120 H, the returns filed contained all the necessary data to enable the Commissioner to compute petitioners’ liability for personal holding company surtax. In making this contention, petitioners also rely on *Germantown Trust Co.*, *supra*, above discussed in connection with the statute of limitations issue. We think our discussion under the statute of limitations issue is equally applicable here.

In the Board’s recent decision in *Olean Times Publishing Co.*, 42 B. T. A. 1277, among other things, we said:

Petitioner filed no personal holding company return, and hence the penalty of 25 percent imposed by the Revenue Act of 1936, section 291, is mandatory. Reasonable cause is only effective to avoid the penalty if the return is delayed—not when the return is omitted en-

tirely, Alex Holmstrom, 35 B. T. A. 1092; dismissed, 94 Fed. (2d) 747; National Contracting Co. v. Commissioner, 105 Fed. (2d) 488. This is true as to a personal holding company return even though an income tax return has been filed, Collateral Mortgage & Investment Co., 37 B. T. A. 630; Rotorite Corporation, 40 B. T. A. 1304 (on review C. C. A., 7th Cir.); Lone Pine Lawn Corporation, 41 B. T. A. 638 (on review C. C. A., 2d Cir.).

On the issue as to delinquency penalties, we sustain the Commissioner. See *Noteman v. Welch*, 108 Fed. (2d) 206.

Issue (k).—Petitioners do not press issue (k) in their brief and it will be considered as abandoned. This assignment of error raised the issue that the Commissioner was estopped by his past acts and conduct from asserting any claim of liability against Technicraft for [57] surtax on personal holding company or penalties thereon. Even if the issue be not considered as abandoned, it is clear that the evidence in the record does not sustain it. There is nothing to show that the Commissioner is estopped.

Reviewed by the Board.

Decision will be entered under Rule 50.

Van Fossan, dissenting:

I believe this case is controlled by the decision of the Supreme Court in *Germantown Trust Co. v. Commissioner*, 309 U. S. 304. [58]

[Title of Board and Cause.]

Docket Nos. 99829, 99830. Promulgated September 25, 1941.

In determining that part of a distribution in liquidation which is "properly chargeable to the earnings or profits accumulated after February 28, 1913" as that term is used in section 27 (f) of the Revenue Act of 1936, held, that all liabilities, including Federal income and surtaxes and penalties, which are proper accruals must first be accrued and deducted from such earnings or profits accumulated after February 28, 1913; held, further, that the Commissioner is in error in contending that the deficiency and penalty which he has determined against petitioner for 1937 should be accrued and deducted from such earnings and profits when, in fact under the Board's decision, there will be no deficiency and penalty for 1937 but on the contrary there will be an overassessment.

Raphael Dechter, Esq., for the petitioners.

E. A. Tonjes, Esq., and Alva C. Baird, Esq., for the respondent.

SUPPLEMENTAL OPINION

Black:

This is a reconsideration of issues (g) and (h) of our report promulgated January 31, 1941, in the

above entitled proceedings. See 43 B. T. A. 463. In this report we said in part:

From petitioner's exhibit 28, introduced in evidence by agreement between the parties, Technicraft's earned surplus, at the time of its merger with the Lane-Wells Co. of Delaware, August 31, 1937, was \$35,660.84 and not \$65,-814.75 as alleged in its assignment of error. The correct amount of Technicraft's earned surplus transferred to the Lane-Wells Co. of Delaware in the reorganization should be used in a recomputation under Rule 50.

In our findings of fact we made a finding that Technicraft's balance sheets showed total assets in excess of total liabilities on August 31, 1937, of \$155,660.84. The evidence for this finding was petitioner's [59] Exhibit 28, which also showed such net assets of \$155,660.84 to be represented by or made up of the following items:

Capital stock	\$25,000.00
Appropriated surplus	75,000.00
Surplus account before charging dividends	10,060.47
Income account—year to date.....	85,600.37
Dividends	(40,000.00)
	<hr/>
	.155,660.84

In our report promulgated January 31, 1941, we arrived at Technicraft's earned surplus of \$55,-660.84 by taking the net result of the last three items shown in the immediately preceding paragraph. If Technicraft's earned surplus, at the time of its merger with the Lane-Wells Co. of

Delaware, August 31, 1937" were at least the amount of \$65,814.75, it would not be liable under Credit Alliance Corporation, 42 B. T. A. 1020; affd., — Fed. (2d) — (July 21, 1941), for the calendar year 1937 for any surtax on undistributed profits under section 14 of the Revenue Act of 1936 or for any surtax on personal holding companies under section 351 of the Revenue Act of 1936 as amended by section 1 of the Revenue Act of 1937, and, instead of deficiencies for 1937 of \$1,196.80 and \$40,992.05 and a penalty of \$10,248.01, as determined by respondent, there would be an overassessment for that year. That this is true is demonstrated by the fact that the parties agree that Technicraft's net income for 1937 is \$123,123.24; that its normal tax for 1937 is \$17,308.39; that the tax previously assessed for 1937 was \$27,003.71; and that it is entitled to a dividends paid credit (exclusive of any earned surplus on August 31, 1937) of \$40,000. See sec. 14 (a) and (b), Revenue Act of 1936, and sec. 1, Revenue Act of 1937. In other words, if for 1937 Technicraft's "dividends paid credit" is the amount of \$105,814.75 instead of \$40,000, it will owe no surtaxes for that year, as the following computation illustrates:

Surtax on Undistributed Profits

Net income	\$123,123.24
Minus normal tax, sec. 14 (a) (1) (A).....	17,308.49
Adjusted net income.....	105,814.75
Minus dividends paid credit, sec. 14 (a) (2)	105,814.75
Undistributed net income.....	None

Surtax on Personal Holding Companies

Net income	\$123,123.24
Deduct: Federal income tax, sec. 356(a) (1)	17,308.49

[60]

Adjusted net income.....	\$105,814.75
Minus dividends paid credit, sec. 355 (a)....	105,814.75
Undistributed adjusted net income.....	None

Was Technicraft's earned surplus at the time of its merger with the Lane-Wells Co. of Delaware on August 31, 1937, at least the amount of \$65,814.75?

On May 12, 1941, we granted at the request of both parties a "Joint Motion to Open Record and for the Introduction of Further Evidence." The purpose of the evidence to be introduced was to show the amount of petitioner's earned surplus at the time it transferred its assets to the Lane-Wells Co., in liquidation, in 1937. On May 29, 1941, the parties filed the following stipulation of facts:

It is hereby stipulated and agreed, by and between the parties hereto, through their respective attorneys, that:

1. The item of \$75,000.00, appearing on Petitioners' Exhibit 28, being a "Statement of assets and liabilities as shown by the books of

Technicraft Engineering Corporation as at May 31, 1937, June 30, 1937, July 31, 1937, and August 31, 1937," and described as "appropriated surplus" was set up out of the earnings of Technicraft Engineering Corporation.

2. The said Petitioners' Exhibit 28 does not reflect the liability of the Technicraft Engineering Corporation for the taxes in controversy herein; and the surplus as reflected by said Exhibit 28 has not been reduced by any amount on account of the said taxes in controversy herein, and the books of the said Technicraft Engineering Corporation do not show any reserve for the taxes in controversy.

Upon the basis of this stipulation both parties agree in their briefs that the appropriated surplus of \$75,000 should be added to the earned surplus of \$55,660.84 determined by the Board, thus making as a starting point an earned surplus of \$130,660.84. From this amount, the respondent contends, there should be subtracted as a liability not reflected by Exhibit 28 all the taxes and penalties which he has determined in his deficiency notice in the total amount of \$74,625.59, thus bringing the earned surplus down to \$56,035.25. Petitioner concedes that the \$130,660.84 should be reduced by the taxes and penalties for the years 1934, 1935, and 1936, which in no event will exceed \$22,210.55, which would bring the earned surplus down to \$108,450.29, or \$42,635.54 in excess of the amount of \$65,814.75. The amount of \$65,814.75 was the

sum which the Commissioner determined as petitioner's undistributed income for the year 1937.

Petitioner contends that there should not be any reduction in its earned surplus on account of 1937 taxes because there will be no deficiency under the Board's decision for that year; but that on the contrary there will be an overassessment. It seems clear that this [61] is true. Under the decision of the Board, following Credit Alliance Corporation, *supra*, petitioner will be entitled to a dividends paid credit, under section 27 (f) of the Revenue Act of 1936, of more than the Commissioner has determined to be its undistributed profits for 1937. Cf. *Commissioner v. Kay Manufacturing Co.*, — Fed. (2d) — (Aug. 5, 1941). Therefore, since it is true that there will be no deficiency against petitioner for the year 1937, it follows that its earned surplus should not be reduced by the accrual of any additional tax liability for that year. On this point we sustain petitioner.

Therefore, we find as a fact that Technicraft's earned surplus, at the time of its merger with the Lane-Wells Co. of Delaware, on August 31, 1937, was at least the amount of \$108,450.29 and that this surplus represented earnings and profits accumulated after February 28, 1913.

Issues (g) and (h) of our report promulgated January 31, 1941, are modified accordingly.

Decision will be entered under Rule 50. [62]

United States Board of Tax Appeals
Washington

Docket No. 99829.

LANE-WELLS COMPANY,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the opinion of the Board promulgated January 31, 1941 and the supplemental opinion of the Board promulgated September 25, 1941, the respondent herein on October 22, 1941 having filed a recomputation of tax and the petitioner's counsel on November 4, 1941 having filed objections to the computation of the respondent and also having filed a recomputation statement of its own, and the said objections and recomputation statement having been duly considered, now, therefore, it is

Ordered and Decided: That there is no income tax or penalty liability against petitioner as transferee of Techniraft Engineering Corporation, Transferor, for the calendar year 1937; and that there are liabilities against petitioner as transferee of Techniraft Engineering Corporation, Transferor, in personal holding company surtax and penalties for the calendar years 1934, 1935, 1936 and 1937 as follows:

Year	Liability in tax	25% Penalty
1934	\$3,178.80	\$ 794.70
1935	9,474.53	2,368.63
1936	5,115.11	1,278.78
1937	None	None

Inasmuch as we have this day determined an overpayment of income tax for the year 1937 in favor of the transferor corporation, Technicraft Engineering Corporation, of \$9,695.22, which amount was paid within three years before the filing of the petition (section 809(a), Revenue Act, 1938), petitioner's liability as transferee for the foregoing deficiencies and penalties is reduced by a proper credit of the foregoing overpayment. See section 322, Revenue Act, 1936: It is accordingly adjudged that petitioner is liable as transferee for the resulting balances due, after proper allowance of such credit, plus interest as required by law.

[Seal] (Signed) EUGENE BLACK,
Member.

Enter: .

Entered Nov. 19, 1941. [63]

United States Board of Tax Appeals
Washington

Docket No. 99830

TECHNICRAFT ENGINEERING CORP.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the opinion of the Board promulgated January 31, 1941 and the supplemental opinion of the Board promulgated September 25, 1941, the respondent herein on October 22, 1941 having filed a recomputation of tax and the petitioner's counsel on November 4, 1941 having filed an agreement to such recomputation, now, therefore, it is

Ordered and Decided: That there is an overpayment of income tax for the calendar year 1937 in the amount of \$9,695.22, which amount was paid within three years before the filing of the petition (Sec. 809 (a), Revenue Act of 1938), and no penalty due for said year 1937; and that there are deficiencies in personal holding company surtax and penalties for the calendar years 1934, 1935, 1936 and 1937 as follows:

Year	Deficiency in tax	.25% Penalty
1934	\$3,178.80	\$ 794.70
1935	9,474.53	2,368.63
1936	5,115.11	1,278.78
1937	None	None

[Seal] (Signed) EUGENE BLACK
Member.

Enter:

Entered Nov. 19, 1941. [64]

United States Circuit of Appeals
For the Ninth Circuit

B. T. A. Docket No. 99829

LANE-WELLS COMPANY,

Petitioner on Review,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

PETITION FOR REVIEW BY THE UNITED
STATES CIRCUIT COURT OF APPEALS
FOR THE NINTH CIRCUIT

To the Honorable, the Judges of the United States
Circuit Court of Appeals for the Ninth Circuit:

I.

JURISDICTION

Now comes Lane-Wells Company, a Delaware corporation, by Raphael Dechter, its attorney, and respectfully shows:

That petitioner is a corporation which was organized under and is existing under the laws of the State of Delaware, and which has its principal office at 5610 South Soto Street, Los Angeles, California, hereinafter referred to as "taxpayer". It is agreed that petitioner is the transferee of and successor in interest of Technicraft Engineering Corporation, a dissolved California corporation, hereinafter sometimes referred to as "Technicraft".

The Respondent is the duly qualified and acting

Commissioner of Internal Revenue of the United States, herein referred to as [65] the "Commissioner".

The taxpayer's transferor filed income tax returns for the taxable years 1934, 1935, 1936 and 1937 with the Collector of Internal Revenue for the Sixth Collection District of the State of California, whose office is located within the Ninth Judicial Circuit wherein the taxpayer's transferor did reside.

The Commissioner determined deficiencies in personal holding company surtax and penalties for the years 1934, 1935, 1936 and 1937 against the taxpayer as transferee of Technicraft, as follows:

Year	Surtax	Penalty
1934	\$3,178.80	\$ 794.70
1935	9,474.53	2,368.63
1936	5,115.11	1,278.78
1937	40,992.05	10,248.01

The Commissioner also determined an overassessment of \$21.82 in income tax for 1936 and a deficiency of \$1,196.80 in income tax for 1937. On June 1, 1939, in accordance with the applicable statute, the Commissioner sent to the taxpayer by registered mail a notice of said deficiency.

Within ninety days thereafter the taxpayer filed a petition for a redetermination of said liability with the United States Board of Tax Appeals. Said case was consolidated for hearing and decision with the appeal of Technicraft Engineering Corp., in U. S. Board of Tax Appeals, Docket No. 99830, and both cases were simultaneously heard by the Board. On January 31, 1941, the Board promulgated its

findings and opinion in said proceeding; on September 25, 1941, the Board promulgated a supplemental opinion modifying some of its former findings and conclusions; and on November 19, 1941, the Board entered a judgment and final order [66] of redetermination wherein and whereby it was ordered and decided that there is no income tax or penalty liability against the taxpayer or its transferor for the calendar year 1937; and that there are liabilities against the taxpayer and its transferor in personal holding company surtax and penalties for the calendar years 1934, 1935, 1936 and 1937, as follows:

Taxable year ended:	Surtax	Penalty 25%
12/31/34	\$3,178.80	794.70
12/31/35	9,474.53	2,368.63
12/31/36	5,115.11	1,278.78

and that said liability for the foregoing deficiencies and penalties is to be properly reduced by a credit for overpayment of income tax for the year 1937 in the amount of \$9,695.22.

II.

NATURE OF CONTROVERSY

The nature of the controversy is as follows: The Commissioner contends that during the calendar years 1934, 1935, 1936 and part of 1937, Technicraft was a personal holding company within the meaning of that term as defined in the Revenue Act. Up to June 1, 1937, all of the corporate stock of Technicraft was owned in equal amounts by four persons, to-wit: W. G. Lane, Hazel T. Lane (husband and

wife) and Walter T. Wells and Mary P. Wells (husband and wife). After June 1, 1937, on which date Technicraft was merged in a reorganization with several other companies similarly owned by the same parties, all of Technicraft's stock was owned by Lane-Wells Company, a Delaware corporation. Technicraft was one of [67] five corporations, the stock of each of which was held in the same manner and in its entirety by Messrs. Wells and Lane and their respective wives. At all times prior to the reorganization all of these corporations, with the exception of Technicraft, were engaged in the performance of various skilled, technical services in the oil industry, particularly the service of gun perforating. In addition to such rendition of services, all of these related corporations (except Technicraft) were engaged also in the manufacture and sale of various products used in the oil industry. At all times after March, 1934, at which time it commenced business operations, Technicraft was engaged in engineering, research, and development work.

When the business of their corporations was first launched, Messrs. Wells and Lane, both of whom were engineers, were cognizant of the necessity of keeping abreast with scientific developments in the oil industry as essential to the success of an oil service business. In December of 1932 they acquired an exclusive license to a patent from one, Sidney Mims, which patent had been issued in the year 1926 and had never proven itself commercially prac-

ticable. Foreseeing the need of scientific research and development on the process of gun perforating, which Mims had sought to develop, and seeing also the need of extensive scientific research and development on various other devices and processes in order to build a successful oil service business, Messrs. Wells and Lane, in December of 1932, agreed that they would set aside 15% of all their income from gun perforating, which 15% would be used to carry on the research, engineering and scientific development of Technicraft. Accordingly, Technicraft became a "laboratory" wherein patents or new processes or devices were secured, developed [68] and passed on to the other Lane-Wells Companies, which were engaged in services, manufacture and sale. In order to provide a convenient method of collecting the 15% of gun perforating income which was to constitute the research fund to be used by Technicraft for the benefit of the various Lane-Wells companies, license agreements were issued from Technicraft, to Lane-Wells Company, a California corporation, Lane-Wells Co. of Oklahoma, an Oklahoma corporation, and Lane-Wells Co. of Texas, a Texas corporation. It was not the intention of the persons involved that these be true license agreements, but rather than that the execution of the license agreements constituted a book-keeping means of providing Technicraft with reimbursement for engineering services rendered. The 15% gun perforating income was collected from Lane-Wells Co. of Oklahoma, Lane-Wells Co. of

Texas, and the entire system of engineering, research and development continued even after the license agreements had expired. Lane-Wells International, another of the related Lane-Wells companies, and which was organized in 1936, received the benefits of engineering development by Technicraft and paid 15% of its income, even without going through the formality of the execution of a similar license agreement.

As a result of scientific development and engineering research and development, gun perforating, which had been commercially impracticable under the Mims patent, became a very successful and profitable business. In addition to the developments in gun perforating, Technicraft engineers explored new fields of endeavor in the oil industry and developed and patented many new products, such as fishing magnets, packers, bridging plugs, packing glands, etc., and many new services such as Strata-graph, ex-raying of cable, underground surveys, etc., all of which were passed on without any [69] further charge to the various Lane-Wells Companies. Technicraft was not a mere depository for patents, but on the other hand, occupied a large building designed for engineering purposes, in which it carried on extensive and elaborate engineering functions. It had on its payroll many experienced engineers.

The Commissioner contends that Technicraft's income was royalty income within the meaning of the Personal Holding Company Act. The taxpayer contends that form must give way to substance and

that the income which Technicraft received as compensation for engineering services is not "royalty" income merely because it was paid through the artificial arrangement of patent license agreements. In the opinion and final decision of the board, the Commissioner's contention above is upheld.

The taxpayer contends that even if the income had been royalty income, Technicraft could not have been a personal holding company during the year of 1937, for the reason that during the latter half of the year 1937 it was no longer doing business, but all of its activities were carried on by the taxpayer as transferee. On June 1, 1937, all of the constituent Lane-Wells companies entered into a reorganization agreement whereby Lane-Wells Company, a Delaware corporation, which had been formed for such purpose, was to issue 250,000 shares of its stock to Messrs. Wells and Lane and their wives respectively, in exchange for all of the stock of the constituent corporations; that as of June 1, 1937, the new Delaware corporation was to take over all of the assets of the constituent corporations as of their value on June 1, 1937, and was to carry on the business of the various corporations. It was provided that the various constituent corporations were to be dissolved in due course. As a result of such agreement, Lane-Wells Company, a Delaware cor- [70] poration, took over the assets of Technicraft as of June 1, 1937, although the mechanics of the plan consumed several months before it was entirely and formally completed. The taxpayer

contends that the fact that formal completion of the reorganization was not consummated until subsequent to June 1, 1937, did not destroy the effectiveness of the agreement that it be given effect as of June 1, 1937, which was also the date of the execution of the reorganization agreement. The Commissioner contends that because the issuance of stock of the taxpayer was delayed due to delay in the issuance of a permit by the Corporation Commissioner of the State of California, that the reorganization cannot therefore be considered as effected as of June 1, 1937. In the opinion and final decision of the Board of Tax Appeals, the Commissioners' contention above is upheld.

As part of the reorganization of June 1, 1937, a sum of not less than \$65,814.75, which was attributable to earned surplus was distributed with the remaining assets of Technicraft to Lane-Wells Company, a Delaware corporation. The taxpayer contends that it is entitled to dividends paid credit for this amount and the Commissioner contends that it is not. In the opinion and final decision of the Board of Tax Appeals, the taxpayer's contention above is upheld. No error on this phase of the Board's decision is hereby specified or alleged.

The taxpayer contended that the three years' statute of limitations barred assessments for the years 1934 and 1935. The Commissioner contended that the failure of Technicraft to file returns on Form 1120-H (personal holding company returns) prevented the statute of limitations from running. It

is conceded that the officers and agents of Technicraft believed in good faith that it [71] was not a personal holding company and, therefore said corporation did not file returns on Form 1120-H. Technicraft fully and completely reported all of its income on Form 1120. In the opinion and final decision of the Board, the Commissioner's contention above was upheld.

The taxpayer contended that the penalties of 25% for Technicraft's failure to file a personal holding company return on Form 1120-H, should not be assessed because Technicraft acted in good faith while the Commissioner contended that the assessment of such penalties was mandatory. In the opinion and final decision of the Board, the Commissioner's contention above is upheld.

III.

ASSIGNMENT OF ERRORS

In making its decision, as aforesaid, the United States Board of Tax Appeals committed the following errors, upon which your petitioner relies as the basis of this proceeding:

1. The Board erred in determining that the taxpayer's transferor was a personal holding company for the years 1934 to 1937, inclusive.
2. The Board erred in failing to determine that the amounts of Technicraft's income designated as royalty were in fact compensation for tangible services rendered to affiliated corporations and as such did not constitute "personal holding company" income.

3. The Board erred in basing its decision in part on the ground that no evidence was introduced to show what portion of Technicraft's income, if any, was derived from engineering services or from non-patentable devices as distinguished from [72] patents, the evidence being clear and convincing that none of the income was attributable to compensation for the use of patents, but that all of said income was for engineering services.

4. The Board erred in its finding that the agreement between W. G. Lane and W. T. Wells to set aside 15% of gross income for research and development was limited only to Lane-Wells Company, a California corporation, the evidence being clear and convincing that it was the agreement that they were to set aside 15% of all their gun perforating business and not limited alone to Lane-Wells Company, a California corporation.

5. The Board erred in failing to hold that the income and deductions reported by Technicraft for the year from June 1, 1937 to August 31, 1937, in fact constituted income and deductions of Lane-Wells Company, a Delaware corporation, which was successor to and transferee of Technicraft.

6. The Board erred in failing to make a finding to the effect that Technicraft's assets were distributed to Lane-Wells Company, a Delaware corporation, as of June 1, 1937, and pursuant to a resolution of Technicraft's Board of Directors on August 27, 1937, which resolution recited that such transfer of assets should be made effective as of June 1, 1937.

7. The Board erred in failing to determine that there was an overassessment of normal income tax against Technieraft for 1937 of \$7,483.16.

8. The Board erred in holding that despite Technieraft's good faith and reasonable cause in not filing returns on Form 1120-H, that the assessment of a penalty was nevertheless mandatory.

9. The Board erred in not holding that the failure of Technieraft to file Form 1120-H for each of the years 1934 to [73] 1937, would prevent the statute of limitations from barring an assessment with respect to the 1934 and 1935 income of Technieraft.

Wherefore, you petitioner prays that the decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals and a transcript be prepared in accordance with the law and rules of said Court and transmitted to the Clerk of said Court for filing and that appropriate action be taken by said Court toward the end that the errors complained of may be reviewed and corrected.

Dated February 13th, 1942.

R. DECHTER

Attorney for Petitioner.

(Duly verified?)

[Endorsed]: U.S.B.T.A. Filed Feb. 16, 1942. [74]

United States Circuit Court of Appeals
For the Ninth Circuit

B. T. A. Docket No. 99830

TECHNICRAFT ENGINEERING CORPORATION,

Petitioner on Review,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

**PETITION FOR REVIEW BY THE UNITED
STATES CIRCUIT OF APPEALS FOR
THE NINTH CIRCUIT**

To the Honorable, the Judges of the United States
Circuit Court of Appeals for the Ninth Circuit:

I.

JURISDICTION

Comes now Technicraft Engineering Corporation, a dissolved California corporation, by Raphael Dechter, its attorney and respectfully shows:

That petitioner is a dissolved corporation which was organized under and dissolved under the laws of the State of California and which had its principal office at 5610 South Soto Street, Los Angeles, California, hereinafter referred to as "taxpayer" and sometimes herein referred to as "Technicraft".

The respondent is the duly qualified and acting Commissioner of Internal Revenue of the United

States, herein referred to as [75] the "Commissioner".

The taxpayer filed income tax returns for the taxable years 1934, 1935, 1936 and 1937, with the Collector of Internal Revenue for the Sixth Collection District of the State of California, whose office is located within the Ninth Judicial Circuit wherein the taxpayer did reside.

The Commissioner determined deficiencies in personal holding company surtax and penalties for the years 1934, 1935, 1936 and 1937 against the taxpayer, as follows:

Year	Surtax	Penalty
1934	\$3,178.80	\$ 794.70
1935	9,474.53	2,368.63
1936	5,115.11	1,278.78
1937	40,992.05	10,248.01

The Commissioner also determined an overassessment of \$21.82 in income tax for 1936 and a deficiency of \$1,196.80 in income tax for 1937. On June 1, 1939, in accordance with the applicable statute, the Commissioner sent to the taxpayer by registered mail a notice of said deficiency.

Within ninety days thereafter the taxpayer filed a petition for a redetermination of said liability with the United States Board of Tax Appeals. Said case was consolidated for hearing and decision with the appeal of Lane-Wells Company as transferee of Technicraft in United States Board of Tax Appeals, Docket No. 99829 and both cases were simultaneously heard by the Board. On January 31, 1941, the Board promulgated its findings and opinion in

said proceeding; on September 25, 1941, the Board promulgated a supplemental opinion modifying some of its former findings and conclusions; and on November 19, 1941, the Board entered a judgment and final order of redetermination wherein and whereby it [76] was ordered and decided that there is no income tax or penalty liability against the taxpayer for the calendar year 1937; and that there are liabilities against the taxpayer in personal holding company surtax and penalties for the calendar years 1934, 1935, 1936 and 1937, as follows:

Taxable year ended 12/31/34	Surtax \$3,178.80	25% Penalty \$ 794.70
Taxable year ended 12/31/35	Surtax 9,474.53	25% Penalty 2,368.63
Taxable year ended 12/31/36	Surtax 5,115.11	25% Penalty 1,278.78

and that said liability for the foregoing deficiencies and penalties is to be properly reduced by a credit for overpayment of income tax for the year 1937 in the amount of \$9,695.22.

II.

NATURE OF CONTROVERSY

The nature of the controversy is as follows:

The Commissioner contends that during the calendar years 1934, 1935, 1936 and part of 1937, the taxpayer was a personal holding company within the meaning of that term as defined in the Revenue Act. Up to June 1, 1937, all of the corporate stock of the taxpayer was owned in equal amounts by four persons, to-wit: W. G. Lane, Hazel T. Lane (husband and wife) and Walter T. Wells and Mary P. Wells (husband and wife). After June 1, 1937, on

which date the taxpayer was merged in a reorganization with several other companies similarly owned by the same parties, all of the taxpayer's stock was owned by Lane-Wells Company, a Delaware corporation. Technicraft was one of five corporations, the stock of each of which was held in the same manner and in its entirety by Messrs. Wells and Lane and their respective wives. At all times prior to the reorganization all of these corporations, with the exception of [77] Technicraft, were engaged in the performance of various skilled technical services in the oil industry, particularly the service of gun perforating. In addition to such rendition of services, all of these related corporations (except Technicraft) were engaged also in the manufacture and sale of various products used in the oil industry. At all times after March, 1934, at which time it commenced business operations, Technicraft was engaged in engineering, research and development work.

When the business of their corporations was first launched, Messrs. Wells and Lane, both of whom were engineers, were cognizant of the necessity of keeping abreast with scientific developments in the oil industry as essential to the success of an oil service business. In December of 1932 they acquired an exclusive license to a patent from one, Sidney Mims, which patent had been issued in the year 1926 and had never proven itself commercially practicable. Foreseeing the need of scientific research and development on the process of gun perforating,

which Mims had sought to develop, and seeing also the need of extensive scientific research and development on various other devices and processes in order to build a successful oil service business, Messrs. Wells and Lane, in December of 1932, agreed that they would set aside 15% of all their income from gun perforating, which 15% would be used to carry on the research, engineering and scientific development of Technicraft. Accordingly, Technicraft became a "laboratory" wherein patents or new processes or devices were secured, developed and passed on to the other Lane-Wells companies, which were engaged in services, manufacture and sale. In order to provide a convenient method of collecting the 15% of gun perforating income which was to constitute the research fund to be used by Technicraft for the benefit of the various Lane-Wells companies, license agreements were [78] issued from Technicraft to Lane-Wells Company, a California corporation, Lane-Wells Co. of Oklahoma, an Oklahoma corporation, and Lane-Wells Co. of Texas, a Texas corporation. It was not the intention of the persons involved that these be true license agreements, but rather than that, the execution of the license agreements, constituted a bookkeeping means of providing Technicraft with reimbursement for engineering services rendered. The 15% of gun perforating income was collected from Lane-Wells Co. of Oklahoma and Lane-Wells Co. of Texas and the entire system of engineering research and development continued even after the license agreements had ex-

pired. Lane-Wells International, another of the related Lane-Wells companies which was organized in 1936 received the benefits of engineering development by Technicraft and paid 15% of its income, even without going through the formality of the execution of a similar license agreement.

As a result of scientific development and engineering research and development, gun perforating, which had been commercially impracticable under the Mims patent, became a very successful and profitable business. In addition to the developments in gun perforating, Technicraft engineers explored new fields of endeavor in the oil industry and developed and patented many new products such as fishing magnets, packers, bridging plugs, packing glands, etc., and many new services such as Strata-graph, ex-raying cable, underground surveys, etc., all of which were passed on without further charge to the various Lane-Wells companies. Technicraft was not a mere depositary for patents, but on the other hand, occupied a large building designed for engineering purposes, in which it carried on extensive and elaborate engineering functions. It had on its payroll many experienced engineers. [79]

The Commissioner contends that Technicraft's income was royalty income within the meaning of the Personal Holding Company Act. The taxpayer contends that form must give way to substance and that the income which it received as compensation for engineering services is not "royalty" income merely because it was paid through the artificial

arrangement of patent license agreements. In the opinion and final decision of the Board, the Commissioner's contention above is upheld.

The taxpayer contends that even if the income had been royalty income, Technicraft could not have been a personal holding company during the year of 1937 for the reason that during the latter half of the year 1937, it was no longer doing business, but all of its activities were carried on by Lane-Wells Company, a Delaware corporation. On June 1, 1937, all of the constituent Lane-Wells companies entered into a reorganization agreement whereby Lane-Wells Company, a Delaware corporation, which had been formed for such purpose, was to issue 250,000 shares of its stock to Messrs. Wells and Lane and their wives respectively, in exchange for all of the stock of the constituent corporations; that as of June 1, 1937, the new Delaware corporation was to take over all of the assets of the constituent corporations as of their value on June 1, 1937, and was to carry on the business of the various corporations. It was provided that the various constituent corporations were to be dissolved in due course. As a result of such agreement, Lane-Wells Company, a Delaware corporation, took over the assets of Technicraft as of June 1, 1937, although the mechanics of the plan consumed several months before it was entirely and formally completed. The taxpayer contends that the fact that formal completion of the reorganization was not consummated until subsequent [80] to June 1, 1937, did not destroy the effectiveness of

the agreement that it be given effect as of June 1, 1937, which was also the date of the execution of the reorganization agreement. The Commissioner contends that because the issuance of stock of Lane-Wells Company (Delaware) was delayed due to delay in the issuance of a permit by the Corporation Commissioner of the State of California, that the reorganization cannot therefore be considered as effected as of June 1, 1937. In the opinion and final decision of the Board of Tax Appeals, the Commissioner's contention above is upheld.

As part of the reorganization of June 1, 1937, a sum of not less than \$65,814.75, which was attributable to earned surplus was distributed with the remaining assets of Technicraft to Lane-Wells Company, a Delaware corporation. The taxpayer contends that it is entitled to dividends paid credit for this amount and the Commissioner contends that it is not. In the opinion and final decision of the Board of Tax Appeals, the taxpayer's contention above is upheld. No error on this phase of the Board's decision is hereby specified or alleged.

The taxpayer contended that the three years statute of limitations barred assessments for the years 1934 and 1935. The Commissioner contended that the failure of Technicraft to file returns on Form 1120-H (personal holding company returns) prevented the statute of limitations from running. It is conceded that the officers and agents of Technicraft believed in good faith that it was not a personal holding company and, therefore, said corporation did not file returns on Form 1120-H.

Technicraft fully and completely reported all of its income on Form 1120. In the opinion and final decision of the Board, the Commissioner's contention above was upheld. [81]

The taxpayer contended that the penalties of 25% for taxpayer's failure to file a personal holding company return on Form 1120-H, should not be assessed because Technicraft acted in good faith while the Commissioner contended that the assessment of the penalties was mandatory. In the opinion and final decision of the Board, the Commissioner's contention above is upheld.

III.

ASSIGNMENT OF ERRORS

In making its decision, as aforesaid, the United States Board of Tax Appeals committed the following errors, upon which your petitioner relies as the basis of this proceeding:

1. The Board erred in determining that the taxpayer was a personal holding company for the years 1934 to 1937 inclusive.

2. The Board erred in failing to determine that the amounts of petitioner's income designated as royalty were in fact compensation for tangible services rendered to affiliated corporations and as such did not constitute "personal holding company" income.

3. The Board erred in basing its decision in part on the ground that no evidence was introduced to show what portion of petitioner's income, if any,

was derived from engineering services or from non-patentable devices as distinguished from patents, the evidence being clear and convincing that none of the income was attributable to compensation for the use of patents, but that all of said income was for engineering services.

4. The Board erred in its finding that the agreement between W. G. Lane and W. T. Wells to set aside 15% of gross income for research and development was limited only to Lane-Wells Company, a California corporation, the evidence being clear and convincing [82] that it was their agreement that they were to set aside 15% of all their gun perforating business and not limited alone to Lane-Wells Company of California.

5. The Board erred in failing to hold that the income and deductions reported by the taxpayer for the year from June 1, 1937 to August 31, 1937, in fact constituted income and deductions of Lane-Wells Company, a Delaware corporation, which was a successor to and transferee of the taxpayer.

6. The Board erred in failing to make a finding to the effect that Technicraft's assets were distributed to Lane-Wells Company, a Delaware corporation as of June 1, 1937, pursuant to a resolution of its Board of Directors on August 27, 1937, which resolution recited that such transfer of assets should be made effective as of June 1, 1937.

7. The Board erred in failing to determine that there was an overassessment of normal income tax against the taxpayer for 1937 of \$7,483.16.

8. The Board erred in holding that despite taxpayer's good faith and reasonable cause in not filing returns on Form 1120-H, that the assessment of a penalty was nevertheless mandatory.

9. The Board erred in holding that the failure of petitioner to file Form 1120-H for each of the years 1934 to 1937, would prevent the statute of limitations from barring an assessment with respect to the 1934 and 1935 income of petitioner.

Wherefore, your petitioner prays that the decision of the Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals and a transcript be prepared in accordance with the law and rules of said Court and transmitted to the Clerk of said Court for filing and that appropriate action be taken by said [83] Court toward the end that the errors complained of may be reviewed and corrected.

Dated February 13th, 1942.

R. DECHTER

Attorney for Petitioner.

(Duly verified.)

[Endorsed]: U.S.B.T.A. Filed Feb. 16, 1942. [84]

[Title of Circuit Court of Appeals and Causes.]

STATEMENT OF EVIDENCE

The above entitled cause came on for hearing at Los Angeles, California, before the Honorable Eugene Black, member of the United States Board of

Tax Appeals, on the 5th day of June, 1940, Raphael Dechter, Esq., appearing on behalf of petitioners, and E. A. Tonjes, Esq., and Alva C. Baird, Esq., appearing on behalf of respondent. Thereupon, the following proceedings were had and the parties, by their attorneys, submitted the following evidence.

Pursuant to stipulation an order was entered consolidating the two cases. [349]

WALTER T. WELLS,

a witness called on behalf of petitioners, being duly sworn, on direct examination, testified as follows:

Direct Examination

I am connected with Lane-Wells Company, a Delaware corporation, as Chairman of the Board of Directors and Vice-President. I am also a stockholder of said corporation owning 8,875 shares. There are 360,000 shares outstanding of said corporation.

Prior to the organization of Lane-Wells Company, a Delaware corporation, I was one of the incorporators and organizers, as well as President of Technicraft Engineering Corporation. The business of Technicraft Engineering Corporation was primarily engineering, as well as research and development and experimental work. It was confined to such business from the time of its organization until its dissolution. Practically all of the work done by Technicraft in engineering, research and development was done for The Lane-Wells Company, a California corporation and the other companies

(Testimony of Walter T. Wells.)

owned by Mr. Lane and myself. Technicraft was organized in December of 1932 and actually started doing business in the spring of 1934. It was inactive from the time of incorporation until the spring of 1934. I am familiar with the exclusive license agreement dated December 21, 1932, between Sidney W. Mims as licensor and Lane-Wells Co. (Calif.) as licensee. The signatures on said document are those of Sidney W. Mims, witnessed by Bradley L. Benson and my signature, witnessed by W. G. Lane. The Mims license agreement refers to the process or method of gun perforating. The Mims patent is a basic patent issued to Mr. Mims in 1926. In December of 1932, we secured the exclusive license agreement on that patent from [350] him.

Thereupon counsel for petitioners offered and there was received in evidence, marked Petitioners' Exhibit 1, the License Agreement dated December 21, 1932, between Sidney W. Mims, as Licensor, and Lane-Wells Co., as Licensee.

PETITIONERS' EXHIBIT No. 1

EXCLUSIVE LICENSE AGREEMENT

This Agreement, made and entered into this 21st day of December, 1932 by and between Sidney W. Mims of the City and County of Los Angeles, State of California, hereinafter referred to as the licensor, and The Lane-Wells Co., a corporation duly organized under the laws of the State of California and

(Testimony of Walter T. Wells.)

having its place of business at 4439 Santa Fe Avenue, in the City and County of Los Angeles, State of California, hereinafter referred to as the licensee,

Witnesseth:

That Whereas said licensor has invented certain method and means for performing well casing, for which he has obtained letters patent of the United States of America, Serial No. 1,582,184, dated April 27th, 1926, and

Whereas the said licensor does hereby warrant that he is the first and sole inventor of the method and means for perforating well casings described in the aforesaid letters patent, and that he is the sole and exclusive owner of said invention and said letters patent, and

Whereas, the licensee is desirous of acquiring the exclusive right to manufacture, use and vend said invention—

Now Therefore It Is Mutually Covenanted and Agreed as Follows:—

1. In consideration of the sum of one hundred dollars (\$100.00) paid by licensee to licensor, receipt of which is hereby acknowledged, and of the covenants and agreements contained herein and of the performance thereof, the licensor does hereby grant the licensee, its successors and assigns, and to its sublicensees, subject to certain restrictions hereinafter written concerning sub-license, the exclusive right, liberty and license to make, use and sell devices embodying the invention patented in and by the aforesaid United States Letters Patent, in and

(Testimony of Walter T. Wells.)

thruout the United States of America, its territories and possessions, under and for the full unexpired term of said letters patent.

2. Licensee agrees to pay licensor in the manner and at the time hereinafter provided, as full consideration for the grant of this license, the sum of one hundred dollars (\$100.00) for each and every month of the fiscal year commencing March 1, 1933 and ending March 1, 1934, and the further sum of two hundred dollars (\$200.00) for each and every calendar month thereafter during the life of this agreement, said monthly payments to be made on the first day of each month.

3. So long as this license remains exclusive, licensee shall be authorized to bring suit in its own name and on its own behalf, or, if required by law, jointly with licensor, and at the expense of licensee, for infringement of said patent under which the licensee is herein licensed, and to collect for its own use all damages, profits and awards of whatever nature recoverable for such infringement. Licensor, however, reserves the right to bring suit in his own name, or jointly with the licensee if required by law, and at licensor's expense, in case the licensee does not do so, to enjoin the unlicensed use of the invention covered by said patent, and to collect for his own use all damages, profits and awards recoverable therein.

4. The Licensee, The Lane-Wells Co., hereby acknowledges the validity of the letters patent aforesaid, the ownership thereof by Sidney W. Mims, and

(Testimony of Walter T. Wells.)

agrees not to be a party, directly or indirectly, to any suit or procedure disputing the validity or tending to impair the value of said letters patent or to diminish the enjoyment of the said Sidney W. Mims of his revenue from said letters patent.

5. The Licensee is free to make such modification in the design and construction of said invention as may be deemed expedient by them to best meet the conditions of manufacture and/or sale and/or use, and the monthly payment of royalty by licensee to licensor shall be due and payable for the life of this agreement, irrespective of what form of casing perforating device licensee shall make, use or sell, so long as the same shall come within the scope of the claims of said letters patent.

6. If either party fails to comply with any provision of this agreement by it to be performed, then at any time during such default (except where the same is by reason of strike, riot, fire, storm or other Providential cause), either party may, by written notice specifying such default, demand performance, and upon failure to cure said default within ninety (90) days of such demand, this agreement may be cancelled in writing at the option of the party making the demand for performance.

7. Licensee shall mark each device embodying licensor's invention as follows:— License Notice Patent No. 1,582,184.

8. All sublicenses which may be hereafter granted by licensee to parties outside this agreement, shall contain and include a copy of this agreement

(Testimony of Walter T. Wells.)

in order that said parties shall have notice of the forfeiture provisions herein contained.

9. Licensee shall have the right to assign this license to a corporation to be known as Technicraft Engineering Corp. to be owned and controlled by W. G. Lane and W. T. Wells.

10. Licensee agrees not to sell any devices which come within the scope of licensor's patent, but instead will adopt the policy of licensing, renting and servicing said devices and derive revenue therefrom by license or rental, and not by sale. Should any such sale be contemplated by licensee, permission to make such sale must first be obtained in writing from licensor so to do.

11. This agreement shall be binding upon and shall enure to the benefit of the executors, administrators and assigns of the licensor, and the successors, assigns or legal representatives of the licensee.

In Testimony Whereof, witness the hand of the licensor, and the licensee has caused these presents to be executed in its name by its president, attested by its secretary, and its corporate seal hereto attached.

SIDNEY W. MIMS (Signed)

Licensor.

BRADLEY L. BENSON (Signed)

Witness.

THE LANE-WELLS CO.

By W. T. WELLS (Signed)

Attest: W. G. LANE (Signed)

Secretary.

[Seal]

(Testimony of Walter T. Wells.)

Subscribed in my presence this 21st day of December, 1932.

W. H. COPPER (Signed)

Notary Public in and for Los Angeles County, State of California.

My commission expires May 3rd, 1934.

[Seal]

Recorded

Transfers of Patents

U. S. Patent Office

Dec. 24, 1932

Liner A155 Page 215

Thomas E. Robertson

Commissioner of Patents

[Endorsed]: U.S.B.T.A. Filed Jun. 5, 1940.

Paragraph 9 of the Mims license agreement states that licensee shall have the right to assign the license to a corporation to be known as Technicraft Engineering Corporation, to be owned and controlled by W. G. Lane and Walter T. Wells, The articles of incorporation of Technicraft had been filed some time previous to that. On March 1, 1934, Lane-Wells Company assigned said exclusive license agreement to Technicraft. It was about March 1, 1934 that Technicraft started doing business.

Thereupon counsel for petitioners offered and there was received in evidence, marked Petitioners' Exhibit 2, a copy of Assignment of ex-

(Testimony of Walter T. Wells.)

clusive License Agreement dated March 1, 1934 from Lane-Wells Co. to Technicraft Engineering Corporation.

PETITIONERS' EXHIBIT No. 2

ASSIGNMENT OF EXCLUSIVE LICENSE AGREEMENT.

Liber V159 page 289

Reference is hereby made to that certain agreement dated December 21, 1932 by and between Sidney W. Mins, of Los Angeles, as licensor, and The Lane-Wells Co., as licensee, wherein and whereunder the licensor, as the inventor and owner of letters patent of the United States of America, Serial No. 1,582,184, dated April 27, 1926 covering a certain method and means for perforating well casing, does grant to the licensee the exclusive license and right to make, use and sell devices embodying the invention patented in and by the aforesaid letters patent, and

Whereas, said licensee took said exclusive license in trust and for the benefit of the Technicraft Engineering Corporation,

Now Therefore, in consideration of Ten Dollars (\$10.00) and other good and valuable consideration, receipt whereof is hereby acknowledged, the undersigned, The Lane-Wells Co. a corporation, and being the licensee designated in the above mentioned exclusive license agreement, does hereby sell, transfer, assign and set over unto the Technicraft Engineering Corporation all of its right, title and interest in and

(Testimony of Walter T. Wells.)

to said exclusive license agreement aforementioned and hereby granting to said Technicraft Engineering Corporation all the right, remedies and privileges of any kind to which it may have been entitled as licensee under said exclusive license agreement, hereby authorizing the said licensee to do any and all things in and about said exclusive license agreement in the same manner that the undersigned, The Lane-Wells Co., might or could do.

Dated: this 1st day of March, 1934.

THE LANE-WELLS CO.

By W. T. WELLS, President.

[Seal] By W. G. LANE, Secretary.

State of California

County of Los Angeles—ss.

On this 1st day of March, 1934, before me, Raphael Dechter, a Notary Public in and for said County and State, personally appeared W. T. Wells, known to me to be the President and W. G. Lane, known to me to be the Secretary of The Lane-Wells Co. the corporation that executed the within instrument, and known to me to be the persons who executed the within instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

Witness my hand and official seal.

RAPHAEL DECHTER,

Notary Public in and for the
County of Los Angeles,
State of California.

[Endorsed]: U.S.B.T.A. Filed Jun. 5, 1940.

(Testimony of Walter T. Wells.)

On March 1, 1934, Technicraft executed a sub-license agreement to Lane-Wells Co. This was executed concurrently with the execution of the assignment to Technicraft.

Thereupon counsel for Petitioners offered and there was received in evidence, marked Petitioners' Exhibit 3, Sub-License Agreement between Technicraft Engineering Corp. and Lane-Wells Company, dated March 1, 1934.

PETITIONERS' EXHIBIT No. 3

SUB-LICENSE AGREEMENT

Liber V159 - page 295

Reference is hereby made to that certain exclusive license agreement entered into December 21, 1932, by and between Sidney W. Mims, as licensor, and The Lane-Wells Co., as licensee, covering the exclusive right and license to make, use and sell any and all devices embodying an invention patented in and by letters patent of the United States of America, Serial No. 1,582,184, dated April 27, 1926, and

Reference is made to that certain assignment of exclusive license agreement, dated March 1, 1934, by and between The Lane-Wells Co., a corporation, assignor, and Technicraft Engineering Corporation, assignee,

Now, Therefore, it is agreed between the parties hereto as follows:

(Testimony of Walter T. Wells.)

That the undersigned, Technicraft Engineering Corporation, does hereby grant to The Lane-Wells Co., a corporation, a sub-license hereunder in consideration of the royalty hereinafter provided, and the undersigned does hereby grant by virtue of this sub-license to said Lane-Wells Co. any and all rights, privileges and remedies which it might or could do, exercise or perform under said license agreement, provided, however, that the rights of such sub-licensee under this sub-license shall be restricted to the State of California.

In consideration of the granting of said sub-license, said Lane-Wells Co., as sub-licensee, does hereby agree to pay to the Technicraft Engineering Corporation, as sub-licensor, a royalty of fifteen (15%) per cent of any and all gross receipts derived from the manufacture, sale, rental or use of any device of any kind by virtue of this sub-license agreement, such royalty to be payable on the 20th day of each and every month for the royalties accruing for the month previous. Such royalty checks shall be accompanied by an itemized accounting showing any and all transactions carried on under this sub-license. Sub-licensor shall be entitled to inspect the books of the sub-licensee at any time for the purpose of verifying any accounting given to it.

Pursuant to the original exclusive license agreement, there is attached hereto a copy of said original exclusive license agreement and said sub-license agrees to perform all and singular the terms thereof.

In the event of any default in the terms and provisions of this agreement, including payment of the

(Testimony of Walter T. Wells.)

royalty and the failure to remedy the same after two weeks after written notice of such default said licensor shall have the option in such event to terminate this sub-license agreement.

Dated: This 1st day of March, 1934.

TECHNICRAFT ENGINEERING CORPORATION

By W. T. WELLS,
President.

By W. G. LANE,
Secretary.

Accepted and Approved:

THE LANE-WELLS CO.

By W. T. WELLS,
President.

By W. G. LANE,
Secretary.

[Seal]

State of California

County of Los Angeles—ss.

On this 1st day of March, 1934, before me, Raphael Dechter, a Notary Public in and-for said County and State, personally appeared W. T. Wells, known to me to be the President, and W. G. Lane, known to me to be the Secretary of The Technicraft Engineering Corporation, the corporation that executed the within instrument, and known to me to be the persons who executed the within instrument on behalf of the corporation therein named, and acknowl-

(Testimony of Walter T. Wells.)

edged to me that such corporation executed the same.

Witness my hand and official seal.

RAPHAEL DECHTER,

[Seal]

Notary Public in and for the
County of Los Angeles,
State of California.

Recorded—Transfers of Patents, U. S. Patent Office, May 26, 1934. Liber V159, page 295.

CONWAY P. COE,

~~Commissioner of Patents.~~

[Endorsed]: U.S.B.T.A. Filed Jun. 5, 1940.

As President of both companies, I executed the License Agreement from Technicraft to Lane-Wells Company of Oklahoma dated February 13, 1936. On or about that date Lane-Wells Co., the California corporation, ceased to do business in Oklahoma and in lieu thereof the Lane-Wells Company of Oklahoma commenced doing business within Oklahoma. [351]

Thereupon counsel for Petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 4, License Agreement dated February 13, 1936, between Technicraft Engineering Corporation, as Licensor, and Lane-Wells Company of Oklahoma, as Licensee.

(Testimony of Walter T. Wells.)

PETITIONERS' EXHIBIT No. 4

LICENSE AGREEMENT

Preamble:

This Agreement made and entered into by and between the Technicraft Engineering Corp., a California corporation, having a place of business in Los Angeles, California, hereinafter referred to as the Licensor, and The Lane-Wells Co. of Oklahoma, an Oklahoma corporation, having a place of business at Oklahoma City, Oklahoma, hereinafter referred to as the Licensee:

Witnesseth

Recitals:

Whereas, the Licensor warrants that it has the right to license to others a certain invention hereinafter referred to as Well Casing Perforator embraced in the following patent:

No.—1,582,184

Inventor—Sidney W. Mims

Date—April 27, 1926

Title—Method and Means for Perforating Well Casing

Whereas, the rights of the Licensor herein relative to said patent number 1,582,184 issued to one Sidney W. Mims is evidenced by a certain exclusive license agreement and assignment thereof recorded in the United States Patent Office, Liber V159, page 289;

Whereas, the Licensee is desirous of acquiring a license in the States of Oklahoma, Kansas, Wyom-

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 4 (Continued)

ing, Colorado, and Montana only, to make and purchase for the Licensee's own use and to use but not to sell, rent or lease to others said Well Casing Perforator, subject, however, to certain reservations and conditions to be set forth hereinafter.

Covenant:

Now, Therefore, in consideration of the sum of Ten Dollars (\$10.00) paid by each party to the other upon execution of this agreement, receipt of which is hereby acknowledged, and in further consideration of the herein contained mutual covenants and agreements for the faithful performance thereof, said parties have and do hereby agree as follows:

I. Definitions:

The term "Perforators" shall be construed to mean not only the patent specifically mentioned hereinbefore, but also any and all inventions, applications, patents and any continuations, divisions, and/or reissues thereof and whether in the nature of apparatus or processes which the Licensor now owns or controls or which it may at any time during the life of this agreement own or control and which relate or are accessories to said Perforators. The term "Patent Rights" shall be construed to embrace as a group all the patents and applications herein specified or referred to or implied. The term "gross receipts" shall be construed to mean the total receipts derived in any manner whatsoever from the manufacture and/or use of any and

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 4 (Continued)

all apparatus or processes covered by said Patent Rights without deductions of any kind or character.

II. License:

The Licensor hereby grants and conveys to the Licensee a non-exclusive license in and throughout the States of Oklahoma, Kansas, Wyoming, Colorado, and Montana only, subject to the terms and conditions of this agreement, to make or purchase for the Licensee's own use only, and to use but not to sell, rent, or lease to others said Perforators.

III. Term of License:

This license shall continue in force, unless otherwise cancelled, for a period of one year from the date of execution thereof, and shall thereafter become null and void except that the parties hereto may by further agreement extend or renew this license.

IV. Royalties:

The royalty payments on the Patent Rights herein licensed shall be fifteen percent (15%) of the gross receipts; minimum royalties shall be not less than Seven Hundred and Fifty Dollars (\$750.00) per month.

Royalty payments shall become due and payable to the Licensor on the tenth day of each month for such royalties as have accrued during the preceding month; the first royalty payment hereunder shall become due and payable on the tenth day of the month following execution of this agreement.

(Testimony of Walter T. Wells.)

Petitioners Exhibit No. 4 (Continued)

V. Books of Account:

The Licensee shall keep accurate books of account showing the purchase, manufacture, and/or use of any and all subject matter relating to or embraced in the Patent Rights herein licensed, said books of account to show plainly the name and address of each customer for whom such use was made and the nature thereof. The Licensee shall give the Licensor, or its duly accredited agent, full access to said books of account at all times during conventional business hours both during the term of this agreement and for a period of twelve (12) months after its termination. The Licensee shall deliver with each royalty payment a full and exact duplicate of the entries made in said books of account during the preceding month.

VI. Diligence in Marketing:

Licensee shall use and continue to use reasonable diligence in creating and fulfilling a demand for the apparatus and/or processes embraced in the Patent Rights herein conveyed, to establish and maintain complete and adequate Perforator service throughout the territory herein licensed, and to conduct the business generally with an endeavor to establish and maintain a good reputation for the subject matter herein licensed.

VII. Improvements by Licensee:

Licensee shall disclose to Licensor all inventions, applications, patents, or continuations, divisions

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 4 (Continued)

and/or reissues dominated by the Patent Rights herein defined which the Licensee may now own or control during the life of this agreement, or which may be jointly or solely invented by any officer, executive, agent, or employee of the Licensee; it being understood that the Licensee shall, upon execution of this agreement, enter into the necessary agreements with its officers, executives, agents and employees to give effect to this section.

Upon disclosure of such inventions, applications, patents, or continuations, divisions and/or reissues, dominated by the Patent Rights, the Licensor shall have a forty-five (45) day option period to accept and incorporate the same with the Patent Rights herein licensed; and, if the nature of the subject matter so accepted requires, to file the necessary patent applications thereon at its own expense. Should the Licensor fail to exercise its option, the Licensee shall retain full rights thereto.

VIII. Infringement of Patent Rights:

A. Suit by Licensor—

Should any or all of the Patent Rights herein conveyed be infringed within the territory herein licensed, the Licensor shall at its own expense and within ninety (90) days after being notified in writing by the Licensee institute and prosecute with diligence a suit or suits against such infringers.

B. Suit by Licensee—

Should the Licensor so fail to sue within the time herein specified, or once commencing such suit

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 4 (Continued)

or suits fail to prosecute the matter with due diligence, the Licensee may either cancel this agreement, or file such suit or suits at its own expense, providing however, the Licensor may at any time employ its own counsel who shall conduct such suit or suits jointly with the counsel for Licensee.

C. Proceeds from Suits—

The party hereto conducting such suit or suits shall be entitled to reimbursement for its expense in conjunction therewith, or if both parties should sue jointly, they shall be reimbursed pro rata; should there be a remainder after such reimbursement, the Licensor shall receive a portion of such remainder corresponding to the royalty percentage specified hereinbefore, and the balance shall go to the Licensee; however, nothing herein shall be construed to give the Licensee any rights to reimbursement from or division of any sums derived from infringement occurring outside the territory herein licensed.

IX. Patent Marking:

Licensee shall affix in a conspicuous place or in conjunction with all apparatus embraced in the Patent Rights herein conveyed a patent notice which complies with the requirements of the patent laws of the United States.

X. Acknowledgment of Validity:

Licensee hereby acknowledges the ownership of the Licensor and the Validity of any and all patents

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 4 (Continued)

now or hereafter constituting a part of said Patent Rights and agrees that it will not at any time during the term of this agreement, or after termination thereof, either directly or indirectly contest the validity or ownership of said Licensor of any and all such patents.

XI. Non-Assignability:

This agreement is personal to the Licensee and is non-assignable either in whole or in part except to the heirs or successors in the business and good will of the Licensor.

XII. Previous Agreements:

All previous agreements, if any, between the parties hereto relating to the Patent Rights herein licensed are hereby cancelled and the present agreement is substituted therefor.

XIII. Knowledge of Extraneous Agreements:

The Licensee herein admits full knowledge of the contents and conditions of a license agreement respecting Patent No. 1,582,184 issued to Sidney W. Mims and recorded in the United States Patent Office at Liber V159, Page 289, and shall be bound by and subject to the conditions therein contained.

XIV. Cancellation Because of Breach:

A. Procedure—

Time is the essence of this contract; therefore, should either of the parties hereto fail to comply

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 4 (Continued)

with any provision of this agreement by it to be performed, then at any time during such default (except where the same is by reason of strike, riot, fire, storm, or other providential cause) the injured party may, by written notice specifying the default, demand performance, and upon failure to cure such default within sixty (60) days after such demand, such injured party may cancel this agreement forthwith, or any part thereof, providing the character of the default so permits; however, should the party in default rectify its default within sixty (60) days, this agreement shall continue in full force and effect as if no notice had been given.

B. Repeated Breach—

Should either party hereto repeat its failure to comply with any provision after once being notified of its breach, even though it has once rectified the default, the injured party may cancel the agreement forthwith upon serving written notice to the party in default.

C. Waiver—

Cancellation of this contract shall not work a waiver of any legal or equitable rights or remedies that the injured party may have, or affect any monetary obligation from the defaulting party to the injured party; and failure of an injured party to notify the party in default shall not work a condonation of the offense, or a waiver of the injured

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 4 (Continued)

party's right to terminate this agreement as herein provided.

XV. Cancellation Irrespective of Breach:

Should a petition in bankruptcy be filed by or against the Licensee, or should a receiver be appointed by any Court to control the assets of the Licensee, or should the Licensee make any assignment for the benefit of creditors, or become involved in any proceedings the effect of which would be, if consummated, to transfer any interest herein to any representative of creditors, trustee, or receiver, this agreement shall be ipso facto void in its entirety, and all rights of the Licensee hereunder shall terminate except to complete and close upon all business done, subject to the terms of this agreement.

XVI. Written Notice:

Wherever in this agreement written notice to either party is required, such condition shall be deemed fulfilled upon deposit into the registered mails of the post office of a postpaid envelope addressed to the other party at its regular and established place of business and containing the required notice.

Signed and executed in duplicate this 13th day of February, 1936.

TECHNICRAFT ENGINEERING CORP.

By **WALTER T. WELLS,**
President

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 4 (Continued)

THE LANE-WELLS CO. OF
OKLAHOMA

By WALTER T. WELLS,
President

State of California,
County of Los Angeles—ss.

On this 13th day of February, 1936, before me, the subscriber, personally appeared Walter T. Wells, who being duly sworn, did depose and say that he is a resident of Glendale, California; that he is the President of the Technicraft Engineering Corp., and The Lane-Wells Co. of Oklahoma, which executed the foregoing instrument; that he knows the seals of said Corporations, that the seals affixed to said instrument are said corporate seals; that they were thereunto affixed by order of the Boards of Directors of the respective Corporations and that he signed his name thereto by like order.

F. R. SHUMACK,

Notary Public, in and for
said County and State

My commission expires Dec. 31, 1939.

[Endorsed]: U. S. B. T. A.

Filed June 5, 1940.

(Testimony of Walter T. Wells.)

As President of both companies, I executed a license agreement between Technicraft and The Lane-Wells Co. of Texas, dated February 13, 1936. The Lane-Wells Co. of Texas had started doing a little of this business a few months prior to the execution of the license agreement.

Thereupon counsel for Petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 5, License Agreement between Technicraft Engineering Corporation and The Lane-Wells Company of Texas, dated February 13, 1936.

PETITIONERS' EXHIBIT NO. 5

LICENSE AGREEMENT

Preamble:

This Agreement made and entered into by and between the Technicraft Engineering Corp., a California corporation, having a place of business in Los Angeles, California, hereinafter referred to as the Licensor, and The Lane-Wells Co. of Texas, a Texas corporation, having a place of business at Houston, Texas, hereinafter referred to as the Licensee:

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

WITNESSETH

Recitals:

Whereas, the Licensor warrants that it has the right to license to others a certain invention hereinafter referred to as Well Casing Perforator embraced in the following patent:

No. 1,582,184; Inventor, Sidney W. Mims; Date, April 27, 1926; Title, Method and Means for Perforating Well Casing.

Whereas, the rights of the Licensor herein relative to said patent number 1,582,184 issued to one Sidney W. Mims is evidenced by a certain exclusive license agreement and assignment thereof recorded in the United States Patent Office, Liber V159, Page 289;

Whereas, the Licensee is desirous of acquiring a license in the States of Texas, Louisiana, Mississippi, Arkansas, and New Mexico only, to make and purchase for the Licensee's own use and to use but not to sell, rent, or lease to others said Well Casing Perforator, subject, however, to certain reservations and conditions to be set forth hereinafter.

Covenant:

Now, Therefore, in consideration of the sum of Ten Dollars (\$10.00) paid by each party to the other upon execution of this agreement, receipt of which is hereby acknowledged, and in further consideration of the herein contained mutual covenants and agreements for the faithful performance

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

thereof, said parties have and do hereby agree as follows:

I. Definitions:

The term "Perforators" shall be construed to mean not only the patent specifically mentioned hereinbefore, but also any and all inventions, applications, patents and any continuations, divisions, and/or reissues thereof and whether in the nature of apparatus or processes which the Licensor now owns or controls or which it may at any time during the life of this agreement own or control and which relate or are accessories to said Perforators. The term "Patent Rights" shall be construed to embrace as a group all the patents and applications herein specified or referred to or implied. The term "gross receipts" shall be construed to mean the total receipts derived in any manner whatsoever from the manufacture and/or use of any and all apparatus or processes covered by said Patent Rights without deductions of any kind or character.

II. License:

The Licensor hereby grants and conveys to the Licensee a non-exclusive license in and throughout the States of Texas, Louisiana, Mississippi, Arkansas, and New Mexico only, subject to the terms and conditions of this agreement, to make or purchase for the Licensee's own use only, and to use but not to sell, rent, or lease to others said Perforators.

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

III. Term of License:

This license shall continue in force, unless otherwise cancelled, for a period of one year from the date of execution thereof, and shall thereafter become null and void except that the parties hereto may by further agreement extend or renew this license.

IV. Royalties:

The royalty payments on the Patent Rights herein licensed shall be fifteen percent (15%) of the gross receipts; minimum royalties shall be not less than Fifteen Hundred Dollars (\$1500.00) per month.

Royalty payments shall become due and payable to the Licensor on the tenth day of each month for such royalties as have accrued during the preceding month; the first royalty payment hereunder shall become due and payable on the tenth day of the month following execution of this agreement.

V. Books of Account:

The Licensee shall keep accurate books of account showing the purchase, manufacture, and/or use of any and all subject matter relating to or embraced in the Patent Rights herein licensed, said books of account to show plainly the name and address of each customer for whom such use was made and the nature thereof. The Licensee shall give the Licensor, or its duly accredited agent, full

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

access to said books of account at all times during conventional business hours both during the term of this agreement and for a period of twelve (12) months after its termination: The Licensee shall deliver with each royalty payment a full and exact duplicate of the entries made in said books of account during the preceding month.

VI. Diligence in Marketing:

Licensee shall use and continue to use reasonable diligence in creating and fulfilling a demand for the apparatus and/or processes embraced in the Patent Rights herein conveyed, to establish and maintain complete and adequate Perforator service throughout the territory herein licensed, and to conduct the business generally with an endeavor to establish and maintain a good reputation for the subject matter herein licensed.

VII. Improvements by Licensee:

Licensee shall disclose to Licensor all inventions, applications, patents, or continuations, divisions and/or reissues dominated by the Patent Rights herein defined which the Licensee may now own or control during the life of this agreement, or which may be jointly or solely invented by any officer, executive, agent, or employee of the Licensee; it being understood that the Licensee shall, upon execution of this agreement, enter into the necessary agreements with its officers, executives, agents and employees to give effect to this section.

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

Upon disclosure of such inventions, applications, patents, or continuations, divisions and/or reissues, dominated by the Patent Rights, the Licensor shall have a forty-five (45) day option period to accept and incorporate the same with the Patent Rights herein licensed; and, if the nature of the subject matter so accepted requires, to file the necessary patent applications thereon at its own expense. Should the Licensor fail to exercise its option, the Licensee shall retain full rights thereto.

VIII. Infringement of Patent Rights:

A. Suit by Licensor—

Should any or all of the Patent Rights herein conveyed be infringed within the territory herein licensed, the Licensor shall at its own expense and within ninety (90) days after being notified in writing by the Licensee institute and prosecute with diligence a suit or suits against such infringers.

B. Suit by Licensee—

Should the Licensor so fail to sue within the time herein specified, or once commencing such suit or suits fail to prosecute the matter with due diligence, the Licensee may either cancel this agreement, or file such suit or suits at its own expense, providing however, the Licensor may at any time employ its own counsel who shall conduct such suit or suits jointly with the counsel for Licensee.

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

C. Proceeds from Suits—

The party hereto conducting such suit or suits shall be entitled to reimbursement for its expense in conjunction therewith, or if both parties should sue jointly, they shall be reimbursed *pro rata*; should there be a remainder after such reimbursement, the Licensor shall receive a portion of such remainder corresponding to the royalty percentage specified hereinbefore, and the balance shall go to the Licensee; however, nothing herein shall be construed to give the Licensee any rights to reimbursement from or division of any sums derived from infringement occurring outside the territory herein licensed.

IX. Patent Marking:

Licensee shall affix in a conspicuous place or in conjunction with all apparatus embraced in the Patent Rights herein conveyed a patent notice which complies with the requirements of the patent laws of the United States.

X. Acknowledgment of Validity:

Licensee hereby acknowledges the ownership of the Licensor and the validity of any and all patents now or hereafter constituting a part of said Patent Rights and agrees that it will not at any time during the term of this agreement, or after termination thereof, either directly or indirectly contest the validity or ownership of said Licensor of any and all such patents.

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued).

XI. Non-Assignability:

This agreement is personal to the Licensee and is non-assignable either in whole or in part except to the heirs or successors in the business and good will of the Licensor.

XII. Previous Agreements:

All previous agreements, if any, between the parties hereto relating to the Patent Rights herein licensed are hereby cancelled and the present agreement is substituted therefor.

XIII. Knowledge of Extraneous Agreements:

The Licensee herein admits full knowledge of the contents and conditions of a license agreement respecting Patent No. 1,582,184 issued to Sidney W. Mims and recorded in the United States Patent Office at Liber V159, Page 289, and shall be bound by and subject to the conditions therein contained.

XIV. Cancellation Because of Breach:

A. Procedure—

Time is the essence of this contract; therefore, should either of the parties hereto fail to comply with any provision of this agreement by it to be performed, then at any time during such default (except where the same is by reason of strike, riot, fire, storm, or other providential cause) the injured party may, by written notice specifying the default, demand performance, and upon failure to cure such

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

default within sixty (60) days after such demand; such injured party may cancel this agreement forthwith, or any part thereof, providing the character of the default so permits; however, should the party in default rectify its default within sixty (60) days, this agreement shall continue in full force and effect as if no notice had been given.

B. Repeated Breach—

Should either party hereto repeat its failure to comply with any provision after once being notified of its breach, even though it has once rectified the default, the injured party may cancel the agreement forthwith upon serving written notice to the party in default.

C. Waiver—

Cancellation of this contract shall not work a waiver of any legal or equitable rights or remedies that the injured party may have, or affect any monetary obligation from the defaulting party to the injured party; and failure of an injured party to notify the party in default shall not work a condonation of the offense, or a waiver of the injured party's right to terminate this agreement as herein provided.

XV. Cancellation Irrespective of Breach:

Should a petition in bankruptcy be filed by or against the Licensee, or should a receiver be appointed by any Court to control the assets of the

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

Licensee, or should the Licensee make any assignment for the benefit of creditors, or become involved in any proceedings the effect of which would be, if consummated, to transfer any interest herein to any representative of creditors, trustee, or receiver, this agreement shall be ipso facto void in its entirety, and all rights of the Licensee hereunder shall terminate except to complete and close upon all business done, subject to the terms of this agreement.

XVI. Written Notice:

Wherever in this agreement written notice to either party is required, such condition shall be deemed fulfilled upon deposit into the registered mails of the post office of a postpaid envelope addressed to the other party at its regular and established place of business and containing the required notice.

Signed and executed in duplicate this 13th day of February, 1936.

**TECHNICRAFT ENGINEER-
ING CORP.**

By **WALTER T. WELLS,**

President.

**THE LANE-WELLS CO. OF
TEXAS**

By **WALTER T. WELLS,**

President

(Testimony of Walter T. Wells.)

Petitioners' Exhibit No. 5 (Continued)

State of California,

County of Los Angeles—ss.

On this 13th day of February, 1936, before me, the subscriber, personally appeared Walter T. Wells, who being duly sworn, did depose and say that he is a resident of Glendale, California; that he is the President of the Technicraft Engineering Corp., and The Lane-Wells Co. of Texas, which executed the foregoing instrument; that he knows the seals of said Corporations, that the seals affixed to said instrument are said corporate seals; that they were thereunto affixed by order of the Boards of Directors of the respective Corporations and that he signed his name thereto by like order.

F. R. SHUMACK,

Notary Public in and for said
County and State.

My commission expires Dec. 31, 1939.

[Endorsed]: U. S. B. T. A.

Filed June 5, 1940.

During all of the time that Technicraft did business, Mr. Lane and I, together with our wives, were the owners of all of the stock of the following corporations: Lane-Wells Co., a California corporation, The Lane-Wells Company of Oklahoma, an Oklahoma corporation, The Lane-Wells Company

(Testimony of Walter T. Wells.)

of Texas, a Texas corporation, and Lane-Wells International, Inc., a California corporation. Such stock ownership continued throughout, up until the time that these companies were merged into a new or reorganized company; Lane-Wells Company, a Delaware corporation.

Lane-Wells Co. (California) started out in 1932 originally selling packers and swabs, and swab rubbers purely as a merchandise proposition. We started to find some new products that could be sold in the oil industry either as merchandise or operated as a service. We hit upon the idea for the gun perforator in June, 1932, and started working on it and developing it for oil field service. At that time we organized Technicraft. We organized Technicraft for the purpose, of doing all of the engineering and experimental and ~~[352]~~ research work for the Lane-Wells Co. of California and any other companies that might be organized later on.

Technicraft did all of the experimental work. It bought a lot of expensive test instruments. It built many devices that were tried out, some of them only small scale models. As the model was improved upon, a full size model was eventually built. In some cases when a finished product was developed, Technicraft would build the first full size model and sell it to Lane-Wells Co. This was the case with the Stratagraph panel.

At the same time that Technicraft acquired quite a number of patents and patent applications, Mr.

(Testimony of Walter T. Wells.)

Lane and I agreed that we would assign to Technicraft all of the patentable ideas or patent applications that either of us might have. Over the period of time that Technicraft was in business, I assigned some 27 patents and Mr. Lane assigned some 6 or 8 patents. In addition, there were applications for patents by other employees of Technicraft. All Technicraft employees signed a patent contract with Technicraft whereby they agreed to assign all of their inventions to the company where such inventions were covered by the scope of the company's operations. The business of Lane-Wells Co., a California corporation throughout its period of existence was a merchandise and oil field service business. It consisted of operation of the gun perforator, fishing magnet, fishing tools, Stratagraph, which was an electrical logging for casing, and later on logging on or in open holes. The merchandise included packers of different kinds, liner hangers, bridging plugs and pumping devices.

Lane-Wells of Texas conducted the same type of business in [353] Texas and for a while covered Louisiana. Lane-Wells Co. of Oklahoma operated in Oklahoma territories, in the South, in New Mexico fields, as well as Arkansas and Kansas fields. It conducted a business similar to that of Lane-Wells Co. of California, except that it was confined to the particular area named. Lane-Wells International, Inc., conducted the same type of business but in foreign countries, operating in Columbia, Peru, Trinidad and Venezuela.

(Testimony of Walter T. Wells.)

The purpose of gun perforating is the making of holes in the pipe underneath the ground. A gun perforator is built like a pencil and has barrels and chambers and screws at the side. The chambers and barrels are screwed into the side of the gun which shoots out bullets horizontally, which penetrate the casing and the formation behind the casing. The gun is lowered into the well by means of an electric cable passed over a pulley. The cable goes into a truck which is provided with a hoist and is operated by the truck motor and the operator. There are three essential elements in the operation of this service; to-wit, the hoist, the cable and the gun. Originally, the first purpose of gun perforating was thought to be the perforation of oil sands that had been passed up in the early days of drilling. Our first job consisted of perforating these sands to see if anything had actually been passed up. Since that time, however, many new uses have been developed for the gun and I should say that at least 50% of the oil wells today are completed by the use of the gun perforator.

One of the most important methods of drilling today consists of setting a string of casing in the ground, then pumping cement in the back of the casing to fill all of the space between the casing and the formation. Then using the record obtained by [354] electrologging, we go into the well with the gun perforator and shoot through the casing and the cement in the lower oil producing sands first.

(Testimony of Walter T. Wells.) *

The cement between the casing and formation shuts off all of the water, and if the holes are put in the right place, no water will be produced with the oil. If the holes are put in the wrong place, however, and the water is produced, it then is a relatively simple matter to go in and cement the gun perforated holes and perforate either further down or higher up until the oil zone is made to produce without water. This was not possible in oil well completion prior to the development of the gun perforator.

The type of truck used in gun perforating is not available from any recognized truck or automobile manufacturer. At the time we entered into the license agreement from Mr. Mims and started in the gun perforating business, there was no truck available for use in this particular service. We had to develop the type of truck and the company that did that developing was Technicraft.

We had to develop a power takeoff unit which was installed in the shaft of the truck so that when a lever was thrown in one position the rear wheels were driven by the motor through the transmission and the truck could operate on the highway. Then when we pulled a well, the operator shifted this lever that disconnected the rear wheels from the truck and connected the truck motor to the hoist and thereafter the truck motor constituted the power necessary for hoisting purposes. That was done back of the transmission, so by using the

(Testimony of Walter T. Wells.)

truck transmission we had a hoist with four speeds as well as a reverse speed. The operator in the control compartment of the truck has a brake, [355] which keeps the gun from lowering into the hole too fast. He has a control panel which has the starting switches of a gasoline engine operated motor generator set, which generates current with which to operate the gun. He also has a throttle control with which to control the truck motor and a tank armature to show the number of revolutions to the truck motor so that he can keep track of the speed. The operator has a weight indicator and if the gun should stop any place going down in the hole, the weight indicator would show less weight and he would know it was not going down. The weight indicator is also used to show whether he may get stuck getting out by reflecting excessive weight. The operator has a measuring device which measures the cable. The cable is measured over a sheave connected with a synchronous motor through a cable to the panel in the truck. The operator has a register which shows him the depth of the gun at all times. The operator also has a loud speaker connected through the same cable to a loud speaker on the derrick floor. This enables voice communication between the derrick floor and the truck operator. This type of device is made necessary because ordinarily there is so much noise around an oil well that without some device of this sort it would not be possible to talk back and

(Testimony of Walter T. Wells.)

forth. The operator has some safety switches so that if the gun is loaded and is lying on the derrick floor he cannot fire the gun until the man in charge of the work on the derrick floor closes the switch and he wouldn't close that switch naturally until after the gun was down in the ground.

None of the developments which I have just described were available to it at the time Lane-Wells Co. secured the license [356] agreement from Mr. Mims. They were all developed by Technicraft.

Thereupon counsel for Petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 6, a diagram taken from a catalog of Lane-Wells Company and used by the witness for the purpose of illustrating the foregoing remarks concerning gun perforating.

At the time that Lane-Wells Co. and Technicraft started in business there was no accurate method of measuring depth of oil wells in connection with oil well operations. There were many arbitrary methods. The only method known at the time to determine the depth at the bottom of a string of casing was a latch jack, which was a couple of fingers that went down and caught underneath the end of the tip of the pipe in the hole. Accurate knowledge of depth measurement of an oil well in the conduct of gun perforating operations is extremely important. In many instances it is the difference between having an oil well and a water

(Testimony of Walter T. Wells.)

well. I recall one instance in Texas where we perforated a well for the first time and got nothing but salt water, and it was about a mile and a half away from the main field. We went back a second time, talked things over with the operator and decided it was due to a possible error in our calculations and that the oil sand should be about eight feet deeper than the place we had perforated. We perforated the well a second time. Instead of being able to get 30 holes as we had intended we only got sixteen and the well started flowing and made about 1500 barrels of oil a day. In this instance, a difference of eight feet had meant the difference between a water well and an oil well. In the East Texas fields six inches is enough to throw you off. Lane-Wells companies use a wire [357] line recording sheave for measuring depth, which was developed for the Lane-Wells companies by Technicraft Engineering Corporation.

Neither the weight indicator nor the measuring device were available to Lane-Wells Co. and Technicraft at the time they started in business. They were both devised and perfected by Technicraft. The truck as presently used by the present Lane-Wells Company for gun perforating purposes is substantially as perfected by Technicraft before the merger and organization of the present Lane-Wells Company, but it has many improvements that have been added to it, which improvements were made by the engineering department of the present company.

(Testimony of Walter T. Wells.)

The former Lane-Wells companies, to-wit, Lane-Wells Co. of California, Lane-Wells International, Inc., the Lane-Wells Company of Oklahoma, and Lane-Wells Company of Texas, had no engineering or research departments, and all engineering, research and development was done for them and made available to them by Technicraft. The Mims patent is but one of a number of patents under which gun perforating is conducted by the present Lane-Wells Company. These other patents were developed and perfected by Mr. Lane and myself and by some of the other fellows at Technicraft. Originally some of the applications were owned by Lane-Wells Co. of California. They were later transferred to Technicraft. While Technicraft was doing business, they owned practically all of the patent applications. The work on all of these was done by Technicraft employees.

The steel line running through a packing gland which made possible safe gun perforating by permitting full control of the [358] well during perforating operations was devised by myself through four or five patent applications, a lot of the work having been done by Technicraft engineers under my direction. I received a salary from Technicraft for engineering services, which salary is shown by the tax returns.

The packing gland was devised by Technicraft. It is a device for perforating a well under pressure while it is flowing, such as in the residential sec-

(Testimony of Walter T. Wells.)

tion, and around the capital of Oklahoma, where wells are close to houses, buildings, etc. It is a safety device to keep any gas or oil from leaking out. The shooter's panel on the Lane-Wells truck together with all of the instruments thereon was devised and perfected by Technicraft.

Thereupon counsel for Petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 7, a sheet containing photographs which were used by the witness to illustrate the matters concerning which he had just testified.

Thereupon counsel for petitioners offered and there was received in evidence, marked Petitioners' Exhibit 8, a document containing photograph of the panel in the gun perforating truck.

Petitioners' Exhibits 8 and 9 consisting of documents containing pictures of the inside of a gun perforating truck panel were taken out of the Lane-Wells monthly magazine for May-June, 1940, and a photograph of the inside of a gun perforating truck taken on February 23, 1935.

Technicraft occupied a large building which was designed particularly for Technicraft and in which Lane-Wells occupied office space.

Thereupon counsel for petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 10, consisting of a photo-

(Testimony of Walter T. Wells.)

graph taken of the Technicraft building on November 17, 1936.

Technicraft conceived the idea of x-raying the conductor [359] core of a cable before it was manufactured and laid up in the steel line, thus avoiding failures which had previously resulted from cables being unable to withstand high pressure and the dissolution of rubber in the oil and heat. Technicraft developed an x-ray machine which showed whether or not there were any breaks in the copper conductor and whether the rubber installation was of uniform thickness. The idea was so practical that it was later copied by the General Electric Company. To our knowledge, Technicraft was the first to develop the use of the x-ray machine for that purpose.

Thereupon counsel for petitioners offered and there was received, in evidence, marked Petitioners' Exhibit 11, consisting of a photograph taken on April 29, 1936, and showing the operation of the Technicraft x-ray machine in which the conductor core for cable is being x-rayed.

Technicraft did all of the experimental work on Stratagraph and spent some \$50,000 or \$60,000 on this one development alone. The Stratagraph panel which was developed by Technicraft enabled the lowering of an electrode down into an oil well with the use of the same cable that was used for perforating, and an attempt was then made to measure

(Testimony of Walter T. Wells.)

the natural current that was in the ground. It operated on the theory that different types of formations have different potential value and would let a different amount of current pass through each different formation. As the instrument was pulled out of the well, the recording curve drawing instrument plotted a curve showing the various differences in formation. Technicraft secured a license agreement from Funk and Ennis on the Stratagraph process and in turn permitted the Lane-Wells companies to use the Stratagraph process. I do not think there was any license agreement from Technicraft to the [360] various Lane-Wells companies. Upon receipt of the license agreement from Funk & Ennis, Technicraft undertook to develop the Stratagraph process in the same manner that it did when it acquired the Mims license agreement. Technicraft spent between \$50,000 and \$60,000 over a period from about November of 1935 until about the middle of the year 1937. At the end of that time, the Lane-Wells companies had had quite a number of commercial jobs, but had never been able to prove that the curve produced by Stratagraph was providing any more information than was already known by geology. For example, an oil well in the Oklahoma City field was brought in on the upper sand based upon a Stratagraph curve. However, in checking the engineering subsequently, we learned that our man in charge of that job was a petroleum engineer and probably would not have

(Testimony of Walter T. Wells.)

put the interpretation on the curve had he not known the geology of the field. Technicraft finally concluded that Stratagraph had not been proved commercially and thereupon abandoned the process. Prior to abandoning the Stratagraph process, Technicraft employed engineers from the California Institute of Technology and even referred the matter to a Swedish company in Stockholm, known as the Electrick Molmletning A. B.

Thereupon counsel for petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 12, consisting of a photograph of a Stratagraph panel developed by Technicraft.

Technicraft developed a fishing magnet from which is suspended a cone from a rock bit. The magnet is about seven inches in diameter and the cone weighs sixteen pounds.

The interior of the Technicraft building consisted of a main Technicraft shop, various offices around the shop, an electrical experimental laboratory, a chemical laboratory and an x-ray room [361] for x-raying cable.

Thereupon counsel for petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 13, consisting of a photograph of a portion of the interior of the Technicraft Building.

From time to time Technicraft conducted tests with the gun perforator for the purpose of improv-

(Testimony of Walter T. Wells.)

ing the accuracy and firing ability and for the purpose of improving the penetration of the gun.

It is my opinion that with the Mims license agreement alone, it would not have been possible for Technicraft or the Lane-Wells companies to conduct a successful gun perforating business. Mr. Mims had had his patent from the time he applied for it in 1926 and was not able to accomplish anything with it until we obtained it in 1932. The Mims' patent was a basic patent covering the idea of lowering a gun into a well casing and shooting a bullet out horizontally to perforate the casing. Mims, however, did not know of a steel that was strong enough to withstand the force of the explosion. He did not know how to get enough powder in to get the bullet to go through the pipe. He had no cable on which to run it and had no operating scheme whatsoever. He merely had a broad idea of perforating the casing. Technicraft, in order to perfect the gun filed a great many patent applications on the means of **delayed firing, of sealing the** gun from the intrusion of water, on firing it underground, so that water pressure was at least 10,000 lbs. pressure per square inch on the gun. Technicraft developed and tested the cable, and developed all the accessories which were used in the truck. In fact, Technicraft developed the entire scheme to the point where it was a commercial possibility.

[362]

The electric curve was transmitted through the

(Testimony of Walter T. Wells.)

steel cable. The steel cable was manufactured with the hemp core in the center left out. Technicraft developed a type of copper conductor which could be put in the center in place of the hemp core and secured a patent on that type of construction. This patent on the wire line has been recognized by the American Steel and Wire Company, the Columbia Steel Company and the General Cable Corporation.

The Mims patent itself simply shows a gun with a barrel and a bullet and an electric wire attached to it. It is suspended on an ordinary cable.

At the time of the original license agreement effected between us and Mims, Mr. Lane and I were the officers and directors and all of the stockholders of Technicraft, as well as the Lane-Wells Co. of California. At such time as the Mims license agreement was effected, we did not know how the gun perforator was to be operated, whether it was to be built and sold outright or to be sold as a service, or just how it should be handled. Mr. Lane and I many times that year discussed the formation of a research, engineering and developing company. Mr. Lane had been with the General Electric Company for about 22 years and had had a lot of experience with electrical engineering development. I had been with the Aluminum Company of America and several other large companies doing engineering work. When we entered into our license agreement with Mims, we made up our minds even before that time, that we would set

(Testimony of Walter T. Wells.)

aside a percentage of our income from our business for research and development work. We arbitrarily took 15% because we believed that that would provide sufficient operating capital for Technicraft and we were willing to spend up to 15% [363] on that type of work so that we would always have something new coming out to sell to the oil industry. We had learned that the oil industry is very progressive and that a new thing might be very valuable today and be superseded tomorrow by something new and better. We agreed that we would spend 15% of our income for that type of engineering and research work.

Among the things sold by The Lane-Wells Co. was packers, the patents of which were all held by Technicraft, having been assigned to Technicraft. The improvements thereafter were made by Technicraft and no additional charge was made to Lane-Wells companies for the use of the packers, outside of the 15%, which was provided for by the sublicense agreement on the Mims patent. The only thing that Technicraft received from Lane-Wells Co. was a flat amount of 15% which percentage we picked out because we knew we were going to spread out.

We were going to incorporate in the different states where we did business, and the 15% was arbitrarily taken and we discussed whether we should change it or raise or lower it. No change was ever made and no more license agreements were ever entered into that I recall. Lane-Wells

(Testimony of Walter T. Wells.)

companies received everything from Technicraft for that one charge of 15%.

We had the idea that the 15% would provide a flexible means of collecting an income for Technicraft in proportion to the volume of business done by the companies. As the companies' business went up they would pay more for research work.

Lane-Wells International, Inc., did the same type of business as the other companies, but operated only in foreign countries.

It did about \$100,000 worth of business itself the first [364] year. I do not think there was any license agreement between Technicraft and Lane-Wells International, Inc. Technicraft collected 15% from Lane-Wells International, Inc., the same as it did from the other companies.

Although the license agreements between Technicraft and the Lane-Wells Company of Texas and Lane-Wells of Oklahoma both expired in February of 1937, as far as I know there never was any new license agreements executed between Technicraft and these companies. Despite such termination in February of 1937, Lane-Wells of Oklahoma and Lane-Wells of Texas continued to pay 15% of their gross business to Technicraft.

I am familiar with the signatures on the reorganization agreement dated June 1, 1937, which is signed by myself, my wife, Bill Lane, and Hazel Lane. I recognize my signature as president of Lane-Wells Co., a California corporation, Techni-

(Testimony of Walter T. Wells.)

craft Engineering Corp., Alexander Anderson, Inc., Lane-Wells International, Inc., Lane-Wells Company of Oklahoma, Lane-Wells Company of Texas and Lane-Wells Company, a Delaware corporation; and the signature of B. G. Peters as secretary of Lane-Wells Co. of California, Technicraft Engineering Corp., Lane-Wells International, Inc., Lane-Wells Co. of Oklahoma, Lane-Wells Co. of Texas, and Lane-Wells Company, a Delaware corporation; as well as the signature of Wanda G. McGraw as secretary of Alexander Anderson, Inc. On June 1, 1937, all of the stock of these companies was owned by Mr. Lane and his wife and my wife and myself. Alexander Anderson, Inc., was a corporation, the entire stock of which was acquired by Mr. Lane and myself and our wives sometime after our organization. Thereafter, the development and engineering work for that company was done by [365] Technicraft.

Thereupon counsel for petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 14, consisting of reorganization agreement dated June 1, 1937, hereinabove described.

Prior to the entering into of the reorganization agreement, I had a great many conversations with Mr. Lane with reference to the proposed consolidation. These conversations took place sometimes at his home, some at my home and some at the office of Lane-Wells companies and Technicraft. Some-

(Testimony of Waiter T. Wells.)

time in September of 1936, we went to the Trust Department of the Security Bank and asked their advice as to the effect of the death of one of us under the circumstances of the four of us owning all of the stock in the six corporations, none of it ever having been sold. We were told that we were in bad shape and that they could not tell what would happen. That fall I went to Europe and when I returned I got in touch with Raphael Dechter, after having discussed the matter with Mr. Lane. Mr. Dechter made a study of the situation. It took him several weeks. He finally wrote a report which report I discussed with Mr. Lane. As I recall it, there were two courses open to us. We could effect a reorganization in accordance with the state laws of the different states in which we were incorporated, or we could do so under federal regulations. After we got Mr. Dechter's report, there seemed to be no other way of doing it other than in accordance with the Federal Regulations because of certain obstacles in state law, which he told me about, but which I do not remember. Thereupon I talked to Mr. Hass of Hartley Rogers and Company who were investment bankers and brokers, with reference to the sale of some of our stock because it looked like our company was expanding [356] very rapidly. In fact our business was growing so fast it was a problem to provide the necessary money and personnel to take care of the expansion. I discussed reorganization with Mr.

(Testimony of Walter T. Wells.)

Hass who studied it over and told me to get the details worked out and then he would work out some proposition for selling the stock of the company. Lane and I finally agreed that that was what we would do. That we would turn in all of our stock in all of the corporations and form one company that would take over all of the assets. I depended upon Mr. Dechter to take care of the mechanics of the thing and I depended upon Mr. Jeppson to assume responsibility for the accounting and auditing. Mr. Jeppson was our certified public accountant, who at the time was an independent auditor and made a monthly report to us. I was thoroughly familiar with the entire situation. Every step of the reorganization was discussed with Mr. Hass, Mr. Dechter, and Mr. Jeppson.

After getting a report from Mr. Dechter, who said it would take a little time to get the reorganization worked out; that we could not simply come to one stopping point and start the next day; and in view of the fact that we owned real estate, automobiles, etc.; that we had to transfer stock and secure permits to issue stock, Mr. Lane and I decided to set the first day of June as the time that we would effect the consolidation. This was done in accordance with the advice of Mr. Dechter and Mr. Jeppson. The mechanics and details were to be worked out just as soon as they could after that, Mr. Dechter handling the legal end and Mr. Jeppson the auditing. I told Mr. Dechter to go

(Testimony of Walter T. Wells.)

ahead and write up the best plan, following our many discussions, and that we would make it effective on the 1st day of June and then clean [367] it up as fast as we could after that. Outside of nominal qualifying shares in Texas, all of the stock of the various Lane-Wells companies was owned by Lane and his wife and me and my wife. The consent of no one other than Mr. and Mrs. Lane, Mrs. Wells and myself was required to the agreement of June 1, 1937. Immediately after the execution of the reorganization agreement, we began negotiations with Hartley Rogers and Company for the sale of 60,000 shares of stock to the public in the new corporation. I had many meetings with Mr. Hass and Mr. Rogers immediately following June 1, 1937, and we discussed some type of underwriting agreement or agency basis upon which the sale of the stock could be handled. We entered into an agreement with Hartley Rogers and Company early in August 1937. [368]

Cross-Examination

W. T. Wells:

Technicraft was formed in 1932 and commenced its business activities some time in 1934 and about which time the Mims patent was assigned to it. Most of the business done by Technicraft is not under the Mims patent. Technicraft spent more money on Stratagraph than it did on the Mims patent. After the acquisition of the patent Technicraft engaged in a great many developments all

(Testimony of Walter T. Wells.)

going at the same time. Possibly more activity was going on on the gun perforator than anything else. A little later the reverse was true when there was more concentrated activity on Strata-graph than anything else. One should not confuse the Mims patent and the gun perforating device. The Mims patent was primarily a paper patent. It was a broad idea with no detail to it. In order to develop a gun per- [369] forating process which would operate commercially, it required the development of many other ideas, but it was necessary to have the basic patent to embrace them all. Technicraft entered into agreements with the various Lane-Wells companies whereby they could operate under the Mims patent and all of the rest of the patents in the patent application for a 15% which we called "royalty." The 15% was measured by the amount of business done by the various companies so as to provide a means of giving Technicraft a revenue in proportion to the volume of business that the individual companies were doing. The various Lane-Wells companies did not receive any licenses to the many other patents developed and acquired by Technicraft, but the said Lane-Wells companies were permitted to use them and the compensation that the companies paid to Technicraft was for the use of the patents, the engineering work and all of the research work. Technicraft permitted the Lane-Wells companies to operate under the methods which were patented to or

(Testimony of Walter T. Wells.)

which Technicraft had acquired rights without any written agreement to that effect. About 8 or 10 of these patents related to gun perforating. By 1937 when we filed a registration statement we had 150 patents or patent applications.

The patents developed by Technicraft did not actually make the Mims patent more effective in its operations in view of the fact that the Mims patent covered an idea which could never be made to operate commercially. Under the Mims patent there was no means of sealing the powder. You could not lower the Mims gun down into 10,000 feet of water without getting the powder wet and you cannot fire a gun if the powder is wet. We filed a patent application on the method of sealing the powder, which is not shown in the Mims patent at all. The use of this method was extended to all of the [370] Lane-Wells companies. At the time the Mims patent was licensed to us it had little value. Mims had not done anything with it for eight years and was willing to let us have it for a \$200.00 per month royalty for the lifetime of the patent. The Mims patent had value from an idea standpoint, not from a commercial standpoint. The other patents were valuable for the details to be applied to the Mims patent, but in themselves you could not have operated without the Mims patent. For example, there was nothing in the Mims patent as to how to seal a bullet. We developed such a method. We could not have operated

(Testimony of Walter T. Wells.)

under that one particular patent without having the Mims patent because after all we still were firing the bullet underground.

The income of Technicraft was not based on income from the Mims patent. Technicraft's income was based on use of all patents under that particular group. The Mims patent never became any more valuable because we only had to pay \$200.00 per month for the life of the entire patent irrespective of how much business we did.

Technicraft received its income from the Lane-Wells companies for engineering and development fees. It received income from apparatus that was developed and first sold to Lane-Wells as a piece of merchandise. The 15% constituted a measure covering the engineering service fee. The apparatus was sold at a price determined upon the cost and reasonable amount of overhead for Technicraft as well as a small profit. For instance, if Technicraft developed a switchboard panel for the use of the Stratagraph, Technicraft bought all of the test instruments and owned all of same. For example, air meters, voltmeters and galvanometers and instruments of that sort. After developing the panel, Technicraft did test it and when it reached the point where it was considered to be [371] commercially practical and out of the development stage, Technicraft would build a model for the other Lane-Wells companies. Technicraft received 15% of the income of the Lane-Wells companies

(Testimony of Walter T. Wells.)

and in addition would actually be selling some apparatus to them at a fee besides the 15%. For instance, Technicraft might build 8 or 10 test devices and sell them to Lane-Wells. Then as Lane-Wells developed its manufacturing facilities it would take over the manufacture of those things whereupon Technicraft would cease to supply them. Apparatus was sold and billed separately and collected for separately.

I recognize my signature on the 1937 income tax return of Technicraft. In order to explain the manner in which the return was made of the income for sales of merchandise, I would have to discuss the same with Mr. Jeppson who prepared it. The books of Technicraft are in the courtroom and available.

Referring to the developments of the gun perforating process as [372] indicated on Exhibit 8, I would say about 95% of that development had been reached by the close of 1937. The primary apparatus such as the weight indicator, measuring device, the electrical circuits, the switches, the instruments, were all completed prior to the end of 1937. There might have been about 5% representing minor improvements thereafter. These improvements had been put to practical use as early as 1934. Around the first of October, 1937, there were possibly between 85 and 100 patents owned either by Technicraft or to which Technicraft had license agreements and which were all available to Lane-Wells.

(Testimony of Walter T. Wells.)

Not over 7 or 8 of these related to the basic principal covered by the Mims patent. In making that statement, the cable patents, for example, were not related to the Mims patent because the Mims gun was only one device that could be run on the cable. There were hundreds of other devices. The cable was but one way of operating the Mims gun. It was not the only way. It did not work the Mims gun more efficiently because the Mims gun could not work at all. The Mims gun as shown in the drawing of the Mims patent reflects a very small fragmentary gun lowered on a field cable with an electric wire running down along side of it to furnish the electrical energy, with no means of sealing the water out of the bullet and no way in the world by which the gun could operate deeper than you could under water. As far as it is practicable in oil wells, you might lower the gun into the well, but you could never get it out because your cable would be all tangled and snarled. The Mims patent is very broad. With the Mims patent alone you could not perforate an oil well. Mims never did it.

In addition to the Mims patent we operated under the Lane patent for delayed fire and sealing the cartridge in place, keeping the powder dry. That patent was thought to be of considerable value at [373] the time, although today we can get along without it as we have developed other means. The cable patent developed by Technicraft cannot be

(Testimony of Walter T. Wells.)

said to come under the Mims patent as the cable which Technicraft developed, although it could satisfactorily be used in gun perforating, could be used for a hundred other purposes, just as the truck and hoist could be used for a good many other purposes. The delayed fire and sealing was the most important patent.

We always considered our patent structure as of little value except to keep others from doing the things that we desired to do. The success of gun perforating is not necessarily due to the patents but due to its own success, in that the oil industry found that it could do a lot of things that it previously had been unable to do.

Upon being asked whether I believe that 15% was reasonable compensation for the use of the Mims patent and the other patents used in connection therewith, I believe that there was good value received, but it was never looked on in that light. received, but it was never looked on in that light.

[374]

A packer is a device that is lowered inside of a casing in an oil well with an expansible packing member which expands when set and seals the space between the outer and inner strings of casing. In other words, it is a sealing ring between two strings of casing. It is occasionally used in connection with gun perforating. It has other uses and is an item of merchandise. They are purchased by oil companies and set by the oil companies.

(Testimony of Walter T. Wells.)

Redirect Examination

As of June 1, 1937, there were around seventy-five patents, the use of which was furnished to the Lane-Wells companies by Technicraft. In considering what was reasonable compensation for the use of the patents, I consider \$200.00 per month sufficient for the use of the Mims patent because that is what Technicraft paid for it to Mims. I would consider \$200.00 per month a reasonable royalty for the use of the Mims idea as covered by the Mims patent at the time I got the license agreement from Mims.

In addition to the packer, Technicraft also devised ideas such as bridging plugs, pump units and various other ideas. All of these ideas as well as ideas and processes were made available to the Lane-Wells companies by Technicraft and the only compensation that Technicraft received for developing these ideas, processes and tools was the 15% of the gross gun perforating business done by the Lane-Wells companies.

I had nothing to do with the keeping of the books and records of Technicraft, as I was but an officer of the corporation and the books were kept by Miss Peters and audited by Mr. Jeppson. I gave no directions as to how entries should be made or anything of that [375] nature. Mr. Jeppson prepared income tax returns and I signed them.

The idea expressed by the Mims patent was that the gun would be fired mechanically. It had been

(Testimony of Walter T. Wells.)

tried out as a mechanical gun but none of the ideas worked. It was not until Technicraft developed the Mims patent that it was made available to the public.

LLOYD SPENCER,

a witness called on behalf of the petitioners, being duly sworn, on direct examination, testified as follows:

Direct Examination

I am a patent attorney and have been engaged as such since 1931. I have also been engaged in doing mechanical engineering work. I know Walter T. Wells and had a conversation with him in the spring of 1934 concerning my being employed by Technicraft. That conversation was at Mr. Wells' office on Santa Fe Avenue, and I believe Mr. Wells and myself were the only ones present. After introductions, I told Mr. Wells my qualifications as a patent attorney and as a draftsman. Mr. Wells outlined the type of position open. He told me he wanted a man to handle the patent work of Technicraft because they were developing a research organization and it would require someone to take care of patents that were to be filed and to protect the ideas that were discovered and invented by members of the organization. Mr. Wells said he wanted someone that could help with some of the drafting and research work; someone who could de-

(Testimony of Lloyd Spencer.)

vote full time to the activities of Technicraft. He took me into the shop and showed me some of the things in the [376] process of development and gave me an idea of the further business of the company.

Mr. Wells said he was primarily interested in developing tools for the oil industry. He specifically mentioned the gun perforator and the magnet. At that time he also showed me an idea concerning a refrigerating packer that was in its inception state. I expressed an interest in the possibility of the position and accepted his offer to come to work for the company.

After going to work for Technicraft I observed the nature of the business and operations. Technicraft was engaged in research work, design work on various devices and services for the oil industry, such as gun perforating, magnet and several other ideas. Mr. Wells called my attention to, and in many instances, had me engage in research before the patent office to determine the patentability of many ideas and in some instances to work out more practical designs from crude sketches that were submitted to me. Among the people who worked for Technicraft at that time were James C. Armond, Mr. Zehokke, Mr. Drake, Mr. Turechek, Mr. Bowsky, Mr. Winter, Mr. Solventine, Mr. Wellington and Mr. Barnes. All of these mentioned were engineers. Some may not have been graduate engineers, but they had experience and were hired as engineers.

(Testimony of Lloyd Spencer.)

I have prepared a list of the various inventions that were owned by Technicraft either on which it secured patents or which it abandoned. This list was prepared from the records and files of Technicraft. An example of one of the ideas included, is that of the bridging plug, which is somewhat similar to a packer, except that it does not seal off between the inner tube and an outer one. It is placed in a casing to form a false bottom in the well. The bridging plug resulted in three patents. Technicraft worked on that patent device. [377]

Thereupon counsel for petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 19, a list of patents assigned to Technicraft from the date of the organization of Technicraft up to June 1, 1937.

PETITIONERS' EXHIBIT No. 19

PATENTS OWNED BY TECHNICRAFT ENGINEERING CORP.

Patent No.	Inventor	Invention
2,043,341	G. F. Turechek	Cable head and Method of Construction
2,043,400	W. T. Wells	Conductor Cable
2,043,401	W. T. Wells	Supporting and Conducting Cable and Method of Constructing the same
2,061,862	W. T. Wells	Cable Construction
2,128,547	W. T. Wells	Multiple Conductor Wire Rope
2,167,098	W. T. Wells	Strand-Carried Multiple Conductor Wire Rope
2,133,776	J. C. Bender	Subsurface Prospecting Device

(Testimony of Lloyd Spencer.)

Petitioners' Exhibit No. 19 (Continued)

Patents Owned by Technicraft Engineering Corp.—(Continued)

Patent No.	Inventor	Invention
2142,555	M. C. Bowsky et al	Automatic Compensator for Geophysical Devices
*1710,203	W. H. Bustall	Packer
1734,470	R. B. Kellogg	Packing and Method of Making the Same
1822,412	G. Meyer	Novel Packer for use with Overshot
1859,744	G. Meyer	Packer for Oil Wells
1925,015	W. T. Wells	Formation Packer
1925,016	W. T. Wells	Packer for Oil Wells
1925,017	W. T. Wells	Rat-hole Packer
1926,017	W. T. Wells	Packer
2033,560	W. T. Wells	Refrigerating Packer
2033,561	W. T. Wells	Method of Packing Wells
2033,564	W. T. Wells et al.	By-pass Packer
2052,786	G. Meyer	Well Packer
2076,301	G. Meyer	Multiple Ring Packer
2076,307	W. T. Wells et al.	Bridging Plug
2076,313	A. J. Zschokke	Bridging Plug and Retrieving Tool Therefor
2076,314	A. J. Zschokke	Bridging Plug and Setting Tool Therefor
1582,184	S. W. Mims	Means and Method for Perforating Well Casings
2029,454	W. T. Wells	Means and Method for Perforating Well Casings
2029,478	M. W. Haines	Means and Method for Perforating Deep Wells
2029,490	W. G. Lane	Method and Means for Controlling Deep Well Gunfire for Perforating Casings
2033,562	W. T. Wells	Method of Preparing Oil Wells for Production
2048,451	M. O. Johnston	Casing Perforating Gun
2061,835	M. W. Haines	Ammunition
2062,974	W. G. Lane	Well Casing Perforator

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(Testimony of Lloyd Spencer.)

Petitioners' Exhibit No. 19 (Continued)

Patents Owned by Technicraft Engineering Corp.—(Continued)

Patent No.	Inventor	Invention
2,062,975	W. G. Lane	Gun Type Well Casing Perforator
2,092,317	W. G. Lane	Gun Perforator Cartridge
2,139,104	W. T. Wells	Pressure Equalizing and Surge Relief Device for Gun Perforator
2,142,583	H. C. Yarbrough	Perforating Gun
Re. 20,832	W. T. Wells	Well Heating Device and Method
1,528,805	J. D. Wade	Hydraulic Pumping Jack
1,944,481	W. T. Wells	Setting Tool for Setting a Liner in an Oil Well or the like
1,987,919	W. T. Wells	Oil Well Tool
2,018,163	W. T. Wells	Heat Exchange Apparatus
2,029,491	W. G. Lane	Gun Type Formation Tester
2,033,563	W. T. Wells	Means for Controlling Well Flow
2,037,896	M. W. Haines	Bottom Hole Gas Bean
2,037,938	Lloyd Spencer	Collar Breaker
2,037,935	W. T. Wells	Means for Splitting Pipe Collars in situ
2,043,340	L. C. Tilbury et al.	Well Cleaner
2,061,863	W. T. Wells	Weight and Tension Measuring De- vice
2,061,864	W. T. Wells	Electrically Operated Fishing Tool
2,061,865	W. T. Wells	Water Educator and Method
2,092,316	W. G. Lane	Oil Well Fishing Magnet
2,092,337	Lloyd Spencer	Formation Testing Apparatus
2,092,338	Lloyd Spencer	Formation Tester
2,118,991	G. F. Turechek et al.	Electrohydraulic Fishing Tool

[Endorsed]: U. S. B. T. A. Filed June 5, 1940.

Thereupon counsel for petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 20, a list of abandoned and unfiled inventions owned by Technicraft, which

(Testimony of Lloyd Spencer.)

had been worked upon by Technicraft but which had proven to be unsuccessful or unpatentable.

PETITIONERS' EXHIBIT No. 20

ABANDONED AND UNFILED INVENTIONS OWNED BY TECHNICRAFT ENGINEERING CORP.

Inventor	Invention	Serial No.	Filed
W. T. Wells	Packing Ring and Method of Making Same	614,730	June 1, 1932
W. T. Wells	Method of Opening Oil-bearing Formation to Produce Therefrom	646,613	Dec. 10, 1932
G. F. Turechek	Liquid Level Indicator for Wells	137,005	Apr. 15, 1937
Lloyd Spencer	Well Pressure and Temperature Gauge	85,759	June 17, 1936
E. R. Smith	Pump Valve	742,647	Sept. 4, 1934
H. J. Quintrell	Swab	177,564	Mar. 23, 1927
W. G. Lane	Cable Length and Tension Measuring Device	694,604	Oct. 21, 1933
W. G. Lane	Controllers for Perforator Guns	747,714	Oct. 10, 1934
M. W. Haines	Means and Method of Controlling the Gas-Oil Ratio of a Well	38,242	Aug. 28, 1935
F. M. Collins	Gauge Apparatus for Pressure Wells	281,742	May 31, 1928
J. C. Arnold	Automatic Control Unit	119,049	Jun. 4, 1937
W. T. Wells	Well Control Unit	631,782	Sept. 6, 1932
W. T. Wells	Formation Packer	642,370	Nov. 12, 1932
E. R. Smith	Fishing Magnet Head	—	—
Lloyd Spencer	Refrigerating Means for Wells	—	—
J. D. Wolff	Internal Combustion Engine	—	—
E. R. Smith	Magnetic Bailer	—	—
H. J. Quintrell	Fishing Tool	—	—
Wells & Haines	Well Washer	—	—

[Endorsed]: U. S. B. T. A. Filed June 5, 1940.

(Testimony of Lloyd Spencer.)

Thereupon counsel for petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 21, a list of assignments of inventions and bearing data compiled from the records of Technicraft.

PETITIONERS' EXHIBIT No. 21

ASSIGNMENTS OF INVENTIONS TO TECHNICRAFT ENGINEERING CORP.

Assignee	Invention	Serial or Patent No.	Date Assigned
J. C. Bender	Stratograph	64,484	July 28, 1936
M. C. Bowsky et al.	Automatic Compensator for Geophysical Devices	58,864	Jan. 6, 1936
M. W. Haines	Ammunition	2,061,835	Jan. 4, 1937
M. W. Haines	Means and Method of Per- forating Deep Wells	2,029,478	Jan. 4, 1937
M. W. Haines	Means and Method of Per- forating Deep Wells	—	Sept. 26, 1934
M. W. Haines	Bottom Hole Gas Bean	—	Sept. 26, 1934
W. G. Lane	Gun Type Well Casing Per- forator	31,684	Oct. 17, 1935
W. G. Lane	Gun Perforator Cartridge	31,685	Oct. 17, 1935
W. G. Lane et al.	Controllers for Perforator Guns	747,714	Dec. 28, 1934
T. E. McMahan	Deflecting Tool	130,888	June 25, 1937
G. Meyer	Novel Packer for use with Overshot	1,822,412	July 14, 1936
G. Meyer	Well Packer	19,834	July 14, 1936
G. Meyer	Multiple Ring Packer	19,835	July 14, 1936
G. Meyer	Packer for Oil Wells	1,859,744	May 12, 1934
G. F. Turechek	Gun Unit for Gun Perforators	27,024	Oct. 1, 1935
G. F. Turechek	Cable Head and Method of Construction	740,670	Aug. 27, 1934
E. R. Smith	Pump Valve	—	Aug. 27, 1934
G. F. Turechek et al.	Electrohydraulic Fishing Tool	—	Aug. 27, 1934

(Testimony of Lloyd Spencer.)

Petitioners' Exhibit No. 21 (Continued)

Assignments of Inventions to Technicraft Engineering Corp.—(Contd.)

Assignee	Invention	Serial or Patent No.	Date Assigned
L. C. Tilbury et al.	Well Cleaner	—	Mar. 31, 1934
J. D. Wade	Hydraulic Pumping Jack	1,528,805	May 8, 1936
W. T. Wells	Pressure Equalizing and Surge Relief Device and Method for Gun Perforator	64,006	June 2, 1936
W. T. Wells	Well Heating Device and Method	64,007	June 2, 1936
W. T. Wells	Strand-carried Multiple Conductor Wire Rope	50,651	Jan. 6, 1936
W. T. Wells	Multiple Conductor Wire Rope	41,456	Oct. 2, 1935
W. T. Wells et al.	By-Pass Packer Head	5,044	Apr. 5, 1935
Lloyd Spencer	Collar Breaker	747,803	Apr. 5, 1935
Lloyd Spencer	Formation Testing Apparatus	19,247	Apr. 5, 1935
Lloyd Spencer	Formation Tester	19,248	Apr. 5, 1935
W. T. Wells et al.	Bridging Plug	17,466	Apr. 5, 1935
W. T. Wells	Formation Packer	1,925,015	Oct. 8, 1934
" " "	Packer for Oil Wells	1,925,016	" " "
" " "	Rat-hole Packer	1,925,017	" " "
" " "	Packer	1,926,017	" " "
W. T. Wells	Setting Tool for Setting a Liner in an Oil Well or the like	1,944,481	Oct. 8, 1934
" " "	Conductor Cable and Method of Manufacture	662,901	" " "
" " "	Cable Construction	648,037	" " "
" " "	Oil Well Tool	631,781	" " "
" " "	Packing Ring and Method of Making Same	614,730	" " "
" " "	Weight and Tension Measur- ing Device	694,564	" " "
" " "	Means for Packing Oil Wells and the like; renewed and title changed to Refriger- ating Packer	642,369	" " "

(Testimony of Lloyd Spencer.)

Petitioners' Exhibit No. 21 (Continued)

Assignments of Inventions to Technicraft Engineering Corp.—(Contd.)

Assignee	Invention	Serial or Patent No.	Date Assigned
" " "	Method of Packing Wells	734,170	" " "
" " "	Supporting and Conducting Cable and Method of Constructing the Same	734,169	" " "
" " "	Heat Exchange Apparatus	735,214	" " "
" " "	Water Eductor and Method Electrically Operated Fishing Tool	735,212	" " "
" " "	Means and Method of Perforating Well Casing	735,211	" " "
" " "	Means and Method of Splitting Pipe Collars in situ	734,171	" " "
" " "	Method of Preparing Oil Wells for Production	735,213	" " "
W. T. Wells	Method and Means for Controlling Well Flow	736,533	Oct. 8, 1939
" " "	Oil Well Fishing Magnets	741,399	" " "
W. G. Lane	Ammunition (1/2 Interest)	694,603	" " "
" " "	Packer for Oil Wells	642,407	" " "
" " "	Packer	355,288	" " "
" " "	Method and Means for Controlling Deep Well Gunfire for Perforating Casing	1,710,203	" " "
W. G. Lane	Well Casing Perforator	648,049	" " "
" " "	Gun Type Formation Tester	642,410	Oct. 9, 1939
Lane-Wells Co.	Indicating Means for Wells	741,409	" " "
" " "	Packing and Method of Making the same	1,822,203	" " "
" " "	Bridging Plug and Retrieving Tool therefor	281,742	" " "
A. J. Zschokke	Bridging Plug and Setting Tool therefor	1,734,470	" " "
" " "		31,391	Oct. 1, 1939
A. J. Zschokke		31,392	Oct. 1, 1939

[Endorsed]: U. S. B. T. A. Filed June 5, 1940.

(Testimony of Lloyd Spencer.)

Referring to the names of Bowsky, Turechek and E. R. Smith appearing on the last three exhibits, these people worked for Technicraft and worked in the same room with me. I assume they were paid by Technicraft as I knew they worked for Technicraft.

On some of the other devices that were assigned to Technicraft such as the assignment by M. W. Haines, Technicraft performed work on such process in perfecting or improving it after it had been assigned to Technicraft by Mr. Haines. Referring to the list of assignments, Technicraft utilized labor and expended money in connection with each one of the particular inventions contained in Petitioners' Exhibits 19, 20 and 21.

Cross-Examination

The purpose of Technicraft was to conduct experiments, develop patentable ideas, obtain patents and carry on engineering work so that the devices would have commercial use and value.

I prepared the assignments of patents to Technicraft and prepared them for the signature of the inventors. They thereupon became the property of Technicraft. I am not familiar with the accounting or whether Technicraft received any compensation for such use by [378] the Lane-Wells companies.

Redirect Examination

I know that Technicraft spent time and money on processing tools that were used by Lane-Wells

(Testimony of Lloyd Spencer.)

companies, which were not patentable. Time and money were spent on improvements, the nature of which were not patentable, but which were of use to the Lane-Wells companies. Technicraft engaged in some manufacturing, but it was largely incidental to research, in the sense that after a produce was developed, several were made to see whether or not it was really practicable. Sometimes this is part of research work. It may be commercial or not.

D. S. JEPPSON,

a witness called on behalf of petitioners, being duly sworn, on direct examination, testified as follows:

I am comptroller of Lane-Wells Company and have been acting as such since April of 1939. Prior to that time I was a Certified Public Accountant and had been engaged as such for approximately fifteen years. I was certified by the Board of Accountancy of the State of California and as a Certified Public Accountant, one of my clients was Technicraft Engineering Corporation. I heard Mr. Wells testify that Technicraft received a certain income from the sale of models and apparatuses created by Technicraft in connection with the development of ideas, processes and tools sold to the Lane-Wells companies. As to each individual development, research problem or process, it was given an

(Testimony of D. S. Jeppson.)

account number, and that account was charged with all research, development and engineering expense over a period that the project was active. When models were made, sometimes there were several made before a satisfactory one was [379] developed and sometimes no satisfactory models were ever developed. When these models were made, the cost of labor, materials, and other costs which went into the making of the model, was charged to the proper project account. In certain circumstances, a completed model or models were sold to the Lane-Wells companies and the approximate or estimated cost of that model or models was credited to the project or development account to which it related. It is this approximate cost that Technicraft received from the Lane-Wells companies.

Either I or one of my assistants prepared all of the income tax returns of the various Lane-Wells companies and Technicraft.

Thereupon counsel for petitioners offered, and there was received in evidence, marked Petitioners' Exhibit 22, income tax return of Technicraft Engineering Corporation, for the calendar year 1934.